THE LAW COMMISSION

TRUSTEES' POWERS AND DUTIES

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PART I
INTRODUCTION AND BACKGROUND

BACKGROUND

1.1 Trusteeship is an increasingly specialised task that often requires professional skills that the trustees may not have. As a result of changes both in the way in which financial markets operate and the purposes for which trusts are now employed, the present law is no longer always adequate to enable trustees to administer a trust to the best advantage of the beneficiaries or the objects of the trust. In this Consultation Paper we make provisional proposals which are intended to make it easier for trustees to fulfil their duties and, in particular, to enable them to employ persons with professional expertise in circumstances where at present they cannot. We examine the implied powers of trustees to employ agents, nominees and custodians, to purchase land, to insure trust property and to remunerate a trustee with professional skills.[1] In the light of this examination, we make provisional recommendations for extending their powers.

1.2 As Item 7 of our Sixth Programme of Law Reform,[2] we recommended that an examination be made of three specific aspects of the law of trusts and also such others as might from time to time appear to the examining agency and to the Lord Chancellor's Department to require examination.[3] It was envisaged that for these other unspecified aspects of the law of trusts, the examining agency might be the Law Commission "jointly with one or more other bodies".[4] On 21 November 1995, the Lord Chancellor's Department agreed that Trustees' Powers and Duties should be added to the Law Commission's Trust Programme and that the work might be carried out by the Commission in conjunction with the independent Trust Law Committee.[5] Acting under this Item in our Sixth Programme, the Law Commission, together with the Scottish Law Commission and the Trust Law Committee, have provided detailed advice to HM Treasury on trustees' powers of investment in relation to the possible repeal of the Trustee Investments Act 1961 under the provisions of the Deregulation and Contracting Out Act 1994.[6] The present Consultation Paper, which has been produced in consultation with the Trust Law Committee, is therefore the second project to be undertaken on Trustees' Powers and Duties.

1.3 Trustees may carry out a particular transaction only if the power to do so has been expressly or impliedly conferred on them—

(1) by the instrument creating the trust;

(2) by statute; or

[1] See further, para 1.4 below.

[2] (1995) Law Com No 234.

[3] Item 7(d), p 32.

[4] Law Com No 234, p 32.

[5] The membership of the Trust Law Committee is set out in Appendix B to this Paper.

[6] See Investment Powers of Trustees: A Consultation Document by HM Treasury, May 1996. We have been very grateful for the assistance that we have received from the Northern Ireland Office of Law Reform and the Law Reform Advisory Committee of Northern Ireland in preparing the advice to HM Treasury. For the results of this consultation, see below paras 2.4 and following.

(3) under the general principles of trust law.[7]

1.4 In this Consultation Paper we examine whether the powers which trustees presently have under those principles of trust law in the absence of any such provision in the trust instrument are adequate. In particular, we consider the extent to which trustees may—

(1) delegate all or some of their powers and discretions;

(2) vest trust property in the hands of nominees;

(3) place the documents or indicia of title to trust property in the safekeeping of a custodian;

(4) purchase land for investment, occupation or otherwise;

(5) insure the trust property; and

(6) where they are professionals, charge for their services to the trust.

If the provisional proposals that we make in this Paper in relation to these matters are accepted, the powers of trustees will be significantly widened. The trusts that are most likely to benefit from our proposed changes are well-established trusts (particularly charitable trusts) which were created before such powers were needed, trusts arising out of home-made wills, and trusts arising on an intestacy. The wider powers that we propose in relation to (1) - (3) are likely to be of principal advantage to larger trusts, whereas those that relate to (4) - (6) may be of the greatest benefit to smaller trusts.

1.5 At present, the powers enjoyed under the general principles of trust law derive in part from case law and in part from statute. The relevant statutory powers are to be found primarily in the Trustee Act 1925.[8] The purpose of the trustee legislation that has been enacted from time to time in this country has been to provide a default framework for the administration of trusts.[9] Powers that were commonly conferred in trust instruments at the time of the relevant legislation have been incorporated into statutory form and apply in the absence of an expression of contrary intention.[10] They are given without prejudice to any additional powers that may be conferred by the trust instrument which created the trust.[11]

1.6 This review has been prompted by three main factors. The first is that trustee

[7] The existence of one express power (whether that is given by the trust instrument or by statute) can of course imply another: see, eg, *Re Pratt's Will Trusts* [1943] Ch 326, where a statutory power to invest trust funds "whether at that time in a state of investment or not", was held to imply a power to sell investments. For an example of a power that is implied from the general principles of trust law, see Part IX of this Paper.

[8] Sections 7, 19, 21, 23, 25 and 30. See too Public Trustee Act 1906, s 4. For the text of these and other statutory provisions, see Appendix A.

[9] There has of course been other legislation which regulates trusts, see, eg, the Variation of Trusts Act 1958, the Charities Acts 1992 and 1993 and the Pensions Act 1995.

[10] See Trustee Act 1925, s 69(2); see below, para 6.59.

[11] *Ibid.*

legislation has not been kept up to date and the existing statutory default provisions have long since ceased to give the powers that trustees need to administer a trust effectively and are indeed generally regarded as seriously restrictive.[12] Both the economic and social nature of trusts and the assets that are characteristically held by them are now very different from what they were when the Trustee Act 1925 was enacted.

1.7 Secondly, and following from this, there have been fundamental changes in the way in which investment business is transacted. The principal changes with which we are concerned[13] - which we explain more fully in Part II of this Paper - are as follows—

(1) the introduction in 1995 of five-day rolling settlement in dealings in shares and securities on the London Stock Exchange;[14]

(2) the introduction in 1996 of dematerialised holding and transfer of title to shares and securities listed on the London Stock Exchange under the CREST system;[15]

(3) the use of similar computerised clearing systems in other markets in which trustees may wish to invest;[16] and

(4) the widespread employment of discretionary fund managers to enable full advantage to be taken of the increasingly complex range of investment opportunities.[17]

1.8 We explain in Parts II to IV of this Paper that the default powers that trustees have under the present law may not permit them to take advantage of these changes. Indeed, the speed of change in investment practice has been such that many trusts will not contain the necessary express powers to enable trustees to take full advantage of them.[18] For example, we were told by one well-known firm of practitioners that although it was now normal to include in trust instruments powers to vest trust property in nominees, this was not the case until quite recently even in trust deeds which contained wide investment powers. For reasons that we explain in Part II of this Paper, most trustees will in consequence be unable to take advantage of the much wider investment opportunities that may be available to them.

[12] For the review by the Law Reform Committee in its 23rd Report, The Powers and Duties of Trustees (1982) Cmnd 8733, see below, para 1.9.

[13] Which are only some of the many changes that have taken place in the financial markets over recent years.

[14] See below, para 2.32.

[15] See below, para 2.24.

[16] See below, para 2.12.

[17] We explain the nature of the functions of a discretionary fund manager, below, para 2.18.

[18] In The Law of Trusts: Delegation by Individual Trustees (1994) Law Com No 220, para 1.9, we acknowledged that the subject of collective delegation by trustees was an "important topic" which needed to be considered, taking into account the significant changes that had occurred in the financial markets since the Law Reform Committee had last reviewed it in 1982, and that "it could be a candidate for the Commission's attention when we undertake further work on the law of trusts".

1.9 The third factor is a concern to make the administration of trusts an easier task for trustees to undertake.[19] The obligations of trusteeship are onerous[20] and, in the absence of an express charging clause, may be unremunerated.[21] It may be difficult to find a person who is willing to act as a trustee, whether in respect of a trust created in the lifetime of the settlor or one which arises under his or her will, and whether as first trustee or to replace one who has died or wishes to retire. This difficulty may be particularly acute if the trust is such that it should really be administered by a professional person. Such trusts may end up under the administration of the Public Trustee as trustee of last resort.[22] It may also be desirable on occasions for trustees to be able to delegate some particular aspects of the administration of a trust to one of their number who is a professional rather than employing an agent. This is likely to be easier if such a trustee can be remunerated. If there were a power to pay for the services of a professional trustee, it might also make it easier to find persons who were willing to take on the trusteeship of a trust where a trustee retired or died, without having to have recourse to the Public Trustee. Furthermore, a wider ability to employ agents more generally might engender a greater willingness to act as trustee.[23]

1.10 One concomitant of giving wider powers to trustees is that it may increase the security of those who enter into transactions with trustees as counterparties.[24] Trustees have a right to be indemnified out of the trust fund for expenses properly incurred by them on behalf of the trust.[25] Although they are personally liable on obligations that they enter into as trustees, they can look to the trust fund for reimbursement. If they become insolvent, the creditors of the trust are subrogated to the trustees' personal rights of recourse to the fund.[26] As those rights of recourse can be enforced only if the trustees could have exercised them, they will not be available to a creditor if the transaction was unauthorised or if the trustees were acting in some way in breach of trust.[27] By giving trustees powers which many consider to be necessary if they are to act in the best interests of the beneficiaries, the risk that the transaction may be in

[19] In Part II, we examine the management of a modern trust, particularly in relation to matters of investment.

[20] And have always been so. Lord Hardwicke LC's famous remark in *Knight v Earl of Plymouth* (1747) Dick 120, 126; 21 ER 214, 216, that "a trust is an office necessary in the concerns between man and man, and which, if faithfully discharged, is attended with no small degree of trouble, and anxiety, it is an act of great kindness in any one to accept it", is still true two and a half centuries later.

[21] Where the court appoints a corporation (other than the Public Trustee) as a trustee, it may authorise such remuneration for its services as the court may think fit: Trustee Act 1925, s 42.

[22] See Public Trustee Act 1906, s 5. The Public Trustee has a statutory duty to charge for her services, even though the trust instrument does not contain a charging clause: *ibid*, s 9. See too Public Trustee (Fees) Act 1957.

[23] These considerations have emerged in part as a result of the recent review of the trust functions of the Public Trustee by a committee on which the Law Commission was represented: see Written Answer, *Hansard* (HL) 30 January 1997, vol 577, col 102.

[24] The rights of those who enter into commercial dealings with trustees has become a source of concern, particularly since the collapse of the Maxwell group of companies. It has prompted two papers by interested bodies, "Rights of Creditors Against Trustees and Trust Funds: A Consultation Paper by the Trust Law Committee", and "Financial Dealings with Trustees" by the Financial Law Panel. Both were published in April 1997.

[25] See, eg *Re Grimthorpe, dec'd* [1958] Ch 615, 623.

[26] *Re Frith* [1902] 1 Ch 342, 345, 346.

[27] *Re Johnson* (1880) 15 ChD 548, 552.

breach of trust will be commensurately reduced.[28]

1.11 This Consultation Paper has been written against the background of the recent review that was undertaken by HM Treasury, of trustees' powers of investment and the possible replacement of the powers conferred by the Trustee Investments Act 1961 with the investment powers of a beneficial owner (subject to safeguards).[29] As we explain in Part II,[30] although these proposals received widespread and almost unanimous support on consultation, it was not in fact possible to proceed with the proposals in the form in which they appeared in the Treasury's consultation paper.

1.12 This is not the first occasion that there has been a review of the powers and duties of trustees. They were last considered in 1982 - and were found wanting - by the Law Reform Committee in its Twenty-third Report.[31] Although its proposals were well received when they were published,[32] they were not implemented, and some of them have been overtaken by events.[33] We have however considered carefully both the analysis and the recommendations made by the Committee, and have gratefully adopted a number of their recommendations in making our provisional proposals. As we explain in Part II of this Paper, our review is not as comprehensive as was the Committee's, though we anticipate that we may wish to examine other aspects of trustees' powers and duties at some stage in the future.

THE SCOPE OF THIS CONSULTATION PAPER

1.13 Although this Paper is concerned in part with delegation by trustees, we do not address all aspects of trustees' powers to delegate nor the powers of every type of trustee. First, our concern is with collective and not individual delegation - where all the trustees, acting together, delegate some function to an agent. We exclude from consideration the circumstances where there are two or more trustees and one of them wishes to delegate his or her individual powers or discretions. This is because in our report, Law of Trusts: Delegation by Individual Trustees,[34] we have already examined the powers of such a trustee and have made recommendations for reform which have been accepted by the Government.[35]

1.14 Secondly, in relation to the powers of pension trustees to delegate, our consideration is necessarily conditioned by the provisions of the Pensions Act 1995, which have given

[28] Cf below, para 3.5.

[29] See Investment Powers of Trustees: A Consultation Document by HM Treasury, May 1996; above, para 1.2.

[30] See below, paras 2.4 and following.

[31] The Powers and Duties of Trustees (1982) Cmnd 8733. The Committee, whose Chairman was Lord Scarman (himself a former Chairman of this Commission), was of the greatest distinction, and included the present Lord Chief Justice, Lord Bingham of Cornhill (as he now is).

[32] For comment, see C T Emery, "Delegation by Trustees - Reforming the Law" (1983) 133 NLJ 1095.

[33] Cf R T Bartlett, "The Law Reform Committee's Trust Investment Recommendations - 10 Years On" [1992] Conv 425, 426. In The Law of Trusts: Delegation by Individual Trustees (1994) Law Com No 220, para 1.9, we noted that since the Law Reform Committee had reported, "there have been considerable changes in the financial markets".

[34] (1994) Law Com No 220.

[35] The recommendations will be implemented when a suitable occasion arises.

trustees new delegation powers in relation to investment.[36] We do not consider that it would be appropriate to reconsider this aspect of their powers of delegation so soon after Parliament has reviewed and redefined them. However, the ability of pension trustees to delegate other functions was left to the general law on trustee delegation. Any changes that may be made to trustees' powers of delegation would therefore apply to pension trustees in the absence of either some stipulation to the contrary in the trust deed or some specific statutory provision. We accept that both the special nature of pension trusts and the policies embodied in the Pensions Act 1995 may mean that some modifications have to be made to our proposals in their application to such trusts. We would particularly welcome the views of those with specialist experience in dealing with pension trusts.

1.15 Thirdly, this Paper is concerned with the delegation by trustees collectively of their *administrative* duties and discretions. It does not consider the delegation by trustees of their *dispositive* functions, that is, their obligations to distribute the trust property to those entitled to it under the trust.[37] By contrast, *individual* trustees may delegate *all* their individual discretions and functions, including their dispositive discretions.[38] As we explain below,[39] the statutory powers of trustees operate as default provisions. The distribution of trust property is one of the most essential functions of trusteeship. We consider that trustees should be expected to perform it unless the settlor has expressly provided to the contrary.

APPROACH TO REFORM

1.16 We can see no obvious justification for departing from the two underlying principles on which legislation on trustees' powers has hitherto always been enacted, namely that it should operate only as a default, and that it should embody the current "best practice" adopted by trust draftsmen. Our provisional proposals are therefore based on the powers that are at present commonly conferred on trustees in a well-drafted trust deed. If any of our readers disagree with this approach, we shall be very grateful to hear from them and to consider alternative suggestions.

APPLICABILITY

1.17 The provisional recommendations which we make in this Paper are intended to apply to all trustees and (where relevant) personal representatives, unless the contrary is stated.[40] In this regard we are following the definition of "trustee" found in the Trustee Act 1925.[41] A question has been raised with us by the Charity Commissioners as to whether those proposals which we make which apply to charity trustees ought also to apply to the directors of charitable corporations.

[36] Section 34; considered below, para 3.42.

[37] For the distinction between administrative and dispositive functions, see Perpetuities and Accumulations Act 1964, s 8; and below, para 6.25.

[38] See Trustee Act 1925, s 25; Enduring Powers of Attorney Act 1985, s 3(3); considered below, paras 3.35 and 3.39 respectively.

[39] Para 3.16.

[40] We make a number of recommendations that relate specifically either to pension trusts or to charitable trusts.

[41] Section 68(17) provides that "...the expressions 'trust' and 'trustee' extend to implied and constructive trusts, and to cases where the trustee has a beneficial interest in the trust property, and to the duties incident to the office of a personal representative, and 'trustee' where the context admits, includes a personal representative...".

1.18 Although it has been said that "[t]he legal nature of a corporate charity is not entirely clear",[42] it is in fact now apparent that such corporations are not trustees,[43] though they are analogous to them.[44] They are not therefore subject to the provisions of the Trustee Act 1925.[45] The powers of such corporations are normally defined in the usual way by their memorandum and articles of association. However, such corporations may not have all the powers that are proposed in this Paper. If charitable trusts were to be given such powers, the Charity Commissioners envisage that many charitable corporations would seek to amend their memorandum and articles of association to obtain the same powers.[46] This would require the consent of the Commissioners.[47] As such applications would in these circumstances be granted as a matter of course, there is much to be said for extending the proposed powers to charitable corporations. Those powers would be in addition to those conferred by the memorandum and articles of association of the corporation.

1.19 **We ask whether readers agree that the proposals contained in this Paper should apply to—**

(1) all trustees;

(2) personal representatives; and

(3) directors of charitable corporations to the extent that they apply to charity trustees;

except where it is otherwise stated or where the context otherwise requires.

STRUCTURE OF THE CONSULTATION PAPER

1.20 In Parts II - VI of this Paper we are primarily concerned with the default powers of trustees as a body to delegate their functions. In Part II we explain how, in modern circumstances, they might wish to carry out such functions in order to manage trust assets most effectively. In Parts III and IV we set out in detail what the law in fact permits them to do in the absence of express provision, summarising the criticisms of the present law. To assist readers, Part V contains a critical summary of the law on collective delegation and sets out our thinking on the fundamental issues involved. In the light of this, we make proposals for reform in Part VI. In Part VII we examine critically the default powers of trustees to vest trust property in nominees and to

[42] Hubert Picarda, *The Law and Practice Relating to Charities* (2nd ed 1995) p 382.

[43] See *Liverpool and District Hospital for Diseases of the Heart v Attorney-General* [1981] Ch 193; and *Rabin v Gerson Berger Association Ltd* (1987, unreported, CA). In the latter case, Ralph Gibson LJ said that "a company formed exclusively for charitable purposes does not, by reason only of that attribute, hold its property on trust; it may own property beneficially which, by reason of its constitution, it must apply to its charitable purposes...". We are grateful to the Charity Commissioners for this reference.

[44] *Liverpool and District Hospital for Diseases of the Heart v Attorney-General*, above, at p 209.

[45] Cf *Palmer's Company Law* (25th ed 1992) paras 8.403 - 8.404. Cf Charities Act 1993, s 97(1) which defines "charity trustees" in terms which include directors of a charitable corporation and "trusts" so as to include charitable corporations. This device is adopted to ensure that charitable corporations are made subject to the same regulation as are charitable trusts.

[46] We understand that this would apply in particular to the powers of remuneration provisionally proposed in Part X of this Paper.

[47] Charities Act 1993, s 64(2).

employ custodians and we make proposals to widen those powers. In Part VIII we consider whether all trustees should have the power to purchase land, whether for investment, occupation or otherwise, that is now enjoyed by trustees of land. In Part IX we examine the extent of trustees' powers to insure trust property and make proposals for the reform of the default statutory power to insure. In Part X we consider whether professional charging clauses should become a default power. In Part XI we summarise the issues on which we seek the views of readers.

ACKNOWLEDGEMENTS

1.21 Although this Consultation Paper has been written and researched by the Commission in the usual way, in relation to Parts II - VII we have been assisted by two papers that were either written or commissioned by the Trust Law Committee. The first was prepared by Professor David Hayton and Ms Emma Ford, and the second was written by Mr Richard Nolan, Fellow of St John's College, Cambridge.[48] We wish to express our gratitude to them for their work. We are also indebted for the assistance which we have received from the officers of the Trust Law Committee, Sir John Vinelott, Professor David Hayton and Mr Michael Jacobs,[49] Ms Sarah McGuffick of the Association of Private Client Investment Managers and Stockbrokers ("APCIMS"), Mr Omar Hameed of the Association of British Insurers, Ms Charlotte Black of Brewin Dolphin Bell Lawrie Ltd, the Charity Commissioners, Mr Mark Kirby, Head of Legal Affairs at CREST Co Ltd, Mr Hugh Mercer of counsel,[50] the Public Trustee, Mr Peter Ross, the Director of the Office for the Supervision of Solicitors, and a number of other persons and bodies acknowledged in the course of this Paper.

[48] We would particularly acknowledge his assistance in relation to Part II of this Paper. However, we are grateful to him for clarifying the issues on all matters considered in Parts II - VII.

[49] Mr Jacobs made a number of inquiries on our behalf about dealings in securities for which we are particularly grateful.

[50] Who generously assisted us on a point of European Community law that arose shortly before we went to press.

PART II
MANAGING TRUST ASSETS TODAY

INTRODUCTION

2.1 It is the paramount duty of trustees "to exercise their powers in the best interests of the present and future beneficiaries of the trust".[1] Furthermore—

> [w]hen the purpose of the trust is to provide financial benefits for the beneficiaries, as is usually the case, the best interests of the beneficiaries are normally their best financial interests.[2]

2.2 In this Part, we explain the problems which confront modern trustees who, in seeking to fulfil their paramount duty, wish to invest and manage the trusts in the manner that is likely to secure the most effective results for the beneficiaries or for the purposes of the trust. As we explain in subsequent Parts of this Paper, there is now a mismatch between the default powers which trustees have under the general law and those which they need to have if they are to manage the trust effectively. There are two main constraints upon them. The first is the rule, considered in Parts III and V of this Paper, that prohibits them from delegating their fiduciary discretions. The second is the requirement, explained in Part VII of this Paper, that they retain the ownership of trust assets. This obligation precludes trustees from vesting the title to trust property in a nominee.

2.3 Traditionally, trust assets were invested in land, mortgages and government stocks. In the absence of any express power in the trust instrument, the purchase of equities was not generally permissible until the enactment of the Trustee Investments Act 1961. That Act continued the ancient policy of imposing restrictions on the range of investments that trustees might select.[3] At the same time, it imposed restrictions on the proportion of a trust fund that might be invested in wider range investments such as shares.[4]

2.4 In May 1996, HM Treasury issued a Consultation Document[5] in which it was proposed to repeal the Trustee Investments Act 1961 under the provisions of the Deregulation and Contracting Out Act 1994 and to give trustees the same investment powers as beneficial owners. Instead of safeguarding beneficiaries by restricting the range of investments that trustees could make, their protection would lie in the duty of the trustees, mentioned above,[6] to act in the best interests of the trust. An essential

1 *Cowan v Scargill* [1985] Ch 270, 286, 287, *per* Megarry V-C. The same principle does of course apply to trusts for purposes which are either charitable or are within one of the exceptional categories of non-charitable purpose trusts which are valid.

2 *Ibid*, at p 287. See too *Harries v The Church Commissioners for England* [1992] 1 WLR 1241, 1246.

3 The policy was originally judicially imposed, but beginning with the enactment of the Law of Property and Trustees Relief Amendment Act 1859 (Lord St Leonards' Act), the restrictions became statutory in form.

4 Trustee Investments Act 1961, s 2.

5 This document was based on advice from the Law Commission (which prepared the draft of the paper for HM Treasury), the Scottish Law Commission and the Trust Law Committee.

6 See para 2.1.

element in fulfilling that duty in relation to a trust of any size would in practice have been the obtaining of investment or management advice.[7] Of the 146 respondents to the Consultation Document, all but two supported the essentials of the proposed scheme.

2.5 In February 1997, a draft Order under the Deregulation and Contracting Out Act 1994 was laid before Parliament. It transpired that it was not possible under the terms of that Act to implement all of the proposals contained in the Consultation Document.[8] Instead of repealing the Trustee Investments Act 1961, the draft Order contained provisions for its amendment. In essence, the effect of the draft Order would have been—

(1) to abolish the requirement that trustees should split the fund into two parts if they wished to invest in wider range investments, such as shares;[9]

(2) to make the obligations to take advice less onerous;[10] and

(3) to remove some of the restrictions which had the effect of excluding certain investments from the list of those which would otherwise have been authorised for trustees.[11]

The draft Deregulation Order was to be supplemented by an Order made under section 12 of the Trustee Investment Act 1961, extending the range of authorised trustee investments.

2.6 As a result of the dissolution of Parliament for the General Election, the Deregulation Order did not complete its passage and was lost.[12] However, the Deregulation Committee of the House of Commons urged HM Treasury "to bring this measure forward as early as possible in the new Parliament".[13] The Select Committee on Delegated Powers and Deregulation of the House of Lords issued a Report on the Draft Order and expressed itself satisfied that the proposal in it met the requirements of the Deregulation and Contracting Out Act 1994.[14] In response to evidence that we submitted to it,[15] the Committee commented that it had—

> also noted the Law Commission's hope that its current work will lead to new primary legislation on the powers of trustees, and the opportunity that that would provide to codify the reforms set out in the draft Deregulation Order. There is little doubt in our minds that the present proposal is only

[7] On the circumstances in which it is appropriate for trustees to take advice, see *Cowan v Scargill* [1985] Ch 270, 289. Where the trust is small or where there is a professional trustee, there may be no need to take advice.

[8] See the Explanatory Memorandum to the draft Order, para 35.

[9] By repealing s 2 of the 1961 Act.

[10] By amending s 6 of the Act.

[11] By repealing parts of Part IV of Schedule 1 of the Act.

[12] The sixty days required for its Parliamentary consideration was not met.

[13] Fourteenth Report, (1996-97) HC 440, para 3.

[14] Twenty-first Report, (1996-97) HL 70, para 79.

[15] See *ibid*, Annex C.

> a first step in the long-overdue reform of trustee investment law, and that other proposals will follow.[16]

2.7 The main impact of the changes proposed in the draft Deregulation Order, if they are implemented, will be felt primarily in relation to—

(1) trusts arising under home-drawn wills;

(2) cases of intestacy;[17] and

(3) trusts that either pre-date the 1961 Act or were created shortly after its enactment.[18]

As regards professionally drawn trust instruments and wills, it has been the normal practice for many years to include powers which enable trustees to invest as if they were beneficial owners. If the proposals contained in the draft Deregulation Order are eventually implemented, virtually all trustees would enjoy substantially wider investment powers either by express provision in the trust deed or by law. Given that the range and sophistication of investments[19] is now such as to be beyond the knowledge and abilities of most non-professional trustees, it is of the greatest importance that trustees have the necessary powers to manage their portfolios effectively. As a leading American authority on trustee investment law has observed—

> Managing a portfolio of marketable securities is as demanding a specialty as stomach surgery or nuclear engineering. There is no more reason to expect the ordinary individual serving as a trustee to possess the requisite investment expertise than to expect ordinary citizens to possess expertise in gastroenterology or atomic science.[20]

2.8 In the remainder of this Part, we first examine in outline four developments that have taken place in relation to investment in securities which are germane to the issues considered in Parts III - VIII of this Paper. These developments are—

(1) the practice of employing nominees in relation to dealings in securities;[21]

[16] *Ibid*, para 78.

[17] See Administration of Estates Act 1925, s 33 (as amended by Trusts of Land and Appointment of Trustees Act 1996, Sched 2, para 5).

[18] In the period following enactment of the Trustee Investments Act 1961, the powers of investment conferred by it were taken by the courts to be the "normally appropriate powers" (*Re Cooper's Settlement* [1962] Ch 826, 830, *per* Buckley J) that were "prima facie sufficient" (*Re Kolb's Will Trusts* [1962] Ch 531, 540, *per* Cross J). They would not therefore be extended on an application to the court in the absence of special circumstances. It seems likely that there were trusts created at that time which followed that judicial guidance and did not give wider investment powers.

[19] Including of course overseas securities.

[20] John H Langbein, "Reversing the Nondelegation Rule of Trust-Investment Law" 59 Mo LR 105, 110 (1994).

[21] See below, para 2.12.

(2) the widespread employment of discretionary fund managers;[22]

(3) the introduction of the CREST system of settling trades of securities in London and Dublin;[23] and

(4) the introduction of five-day rolling settlement in relation to the purchase of shares and securities on the London Stock Exchange.[24]

In each case, we highlight the particular issues that these developments have thrown up. Secondly, we examine briefly certain matters that may arise where land is held as an investment by a trust.[25] We begin, however, with a brief outline of the law on financial services in so far as it is likely to affect trustees when investing trust funds.

INVESTING IN SECURITIES

Financial services

Introduction

2.9 It is unnecessary for the purposes of this Paper to give any detailed account of the regulatory structure applicable to the financial services industry, which derives from the requirements of the Financial Services Act 1986.[26] However, a little must be said by way of background about the way in which it affects private customers[27] - which will include the great majority of trustees[28] - in relation to investment management. The Act regulates the conduct of investment business in the United Kingdom, which for these purposes now includes—

(1) dealing in, arranging deals in, and managing investments;[29]

(2) giving, offering or agreeing to give investment advice;[30] and

(3) safeguarding and administering (or arranging to safeguard and administer)

[22] See below, para 2.18.

[23] See below, para 2.24. CREST came into operation on 15 July 1996.

[24] To be replaced by three-day rolling settlement in due course. Before five-day rolling settlement was introduced, the period for settlement was ten days. See below, para 2.32.

[25] See below, para 2.35.

[26] As amended by the Companies Act 1989. Those amendments have significantly affected the way in which the regulatory system works.

[27] Who are defined by the Financial Services Core Glossary 1991 (3rd ed) as "(a) a customer who is an individual and who is not acting in the course of carrying on investment business; or (b) unless he is reasonably believed to be an ordinary business investor, a customer who is a small business investor".

[28] A trustee will be a "small business investor" unless the trust has assets which either exceed £10 million or which have done so during the previous two years: *ibid*. If the trust *does* fall within the exception by reason of its size, it will be an "ordinary business investor" and, as such, *not* a private customer.

[29] Financial Services Act 1986, Sched 1, Part II, paras 12, 13, 14.

[30] *Ibid*, para 15.

investments.[31]

Protection of private investors

2.10 The Act is intended to provide a system of protection for all investors.[32] It contains provisions regulating the conduct of investment business[33] and confers wide powers of intervention on the Securities and Investments Board ("SIB"),[34] including (for example) the power to order the transfer to an approved trustee of assets held by an authorised person[35] as a nominee for investors.[36] The rules of the three Self-Regulating Organisations ("SROs") that regulate bodies which may carry on the business of investment management,[37] namely the Investment Management Regulatory Organisation ("IMRO"), the Securities and Futures Authority ("SFA"), and the Personal Investment Authority ("PIA"),[38] contain a further layer of protection for investors generally.[39] For example, the rules provide that a firm "should either avoid any conflict of interest arising or, where conflicts arise, should ensure fair treatment to all its customers by disclosure, internal rules of confidentiality, declining to act or otherwise".[40]

2.11 Private customers enjoy certain additional protection under both the Financial Services Act 1986 itself and the rules of the SROs. Two provisions of the Act (as amended) are particularly important in this regard. First, contraventions of the provisions on the conduct of investment business which cause loss are actionable by private investors.[41] Secondly, the Act makes provision for SIB to establish by rules a compensation scheme "where persons who are or have been authorised persons are unable, or likely to be unable, to satisfy claims in respect of any description of civil liability incurred by them in connection with their investment businesses".[42] The Investors Compensation

[31] *Ibid*, para 13A (added by Financial Services Act 1986 (Extension of Scope of Act) Order 1996, 1996 SI No 2958, cl 3).

[32] We are aware that the Act has not lacked its critics and that some consider that it does not go far enough. It appears that further changes to the regulation of financial markets are likely to be proposed by the European Commission in the near future: see Jonathan Ames, "Directive looms for financial services" (1997) 94/12 LSGaz 12.

[33] Part I, Chapter V.

[34] Part I, Chapter VI.

[35] See Part I, Chapter III.

[36] Section 67.

[37] A person cannot carry on investment business in the United Kingdom unless they are an "authorised person" within Part III of the Act or an "exempted person" within Part IV of the Act: s 3. One of the principal means of becoming an authorised person is to be granted membership of a SRO: s 7.

[38] To the extent that they are relevant to this discussion, the rules of the PIA are based upon the IMRO Rules with necessary modifications. They are not therefore referred to expressly in this discussion.

[39] Formerly, the rules of the SROs tracked the requirements of the SIB Core Rules. However, virtually all of those Core Rules have been "dedesignated" by the Financial Services (Dedesignation) Rules and Regulations 1994 (made by SIB). The SROs are not therefore so constrained as to the content of their own rules as they were.

[40] IMRO Rules, rr I-1.3(6), II-3.3(1); SFA Rules, Principles, 6; r 5-29(1).

[41] Sections 62, 62A.

[42] Section 54(1).

Scheme which was established under that provision,[43] applies in practice only in cases of insolvency,[44] and is therefore the line of last (rather than primary) resort. It is in any event subject to an upper limit of £48,000 on any claim for compensation by a private customer[45] in cases of default.[46] Again, the rules of the SROs contain special protection for private customers. These relate in particular to the form and content of customer agreements.[47]

The employment of nominees and custodians

The practice and its advantages

2.12 In a recent consultation paper, HM Treasury commented that "custody is now an integral part of modern investment business and is often seen as best practice".[48] For these purposes, "custody" is to be understood as meaning the safeguarding and administering[49] of another's assets where those include investments.[50] There are many reasons why investors may place their investments in the name of such a nominee or custodian. It is enough to mention just four. First, where an investor retains a traditional portfolio that is not managed by a discretionary fund manager, the nominee may provide an administration service. The nominee collects all the dividends, provides statements for the investor and the necessary paperwork for Inland Revenue purposes. This practice also facilitates any sales of securities in certificated form where (as is commonly the case) the nominee is also the investor's broker (or a related nominee company), because it does not have to obtain the investor's signature on any transfer documents.[51] Secondly, where the portfolio is managed by a discretionary fund manager, it is usual for the title to be vested in a nominee, simply to facilitate the more rapid transfer of securities.[52] Thirdly, although it is in no sense essential, one method of dealing in shares in dematerialised form through the computerised CREST system,[53]

[43] See the Financial Services (Compensation of Investors) Rules 1994 (replacing earlier rules).

[44] *Ibid*, r 2.01.

[45] As we have indicated above, para 2.9, most trustees will, for these purposes, be private customers.

[46] *Ibid*, r 2.07. The figure has not changed since it was introduced in August 1988. The first £30,000 of losses are recoverable in full under the scheme. For additional losses of £20,000, the investor may recover 90% of his or her losses (hence the £48,000 maximum). Nothing is recoverable for losses above £50,000.

[47] See, eg SFA Rules rr 5-23(1), 5-23(2).

[48] Custody: A Consultation Document by HM Treasury (June 1996), para 12(c). This paper sought views on what subsequently became the Financial Services Act 1986 (Extension of Scope of Act) Order 1996, 1996 SI No 2958.

[49] Or arranging for such safeguarding and administration. "Administration" has, for these purposes, its normally understood meaning: see Custody: A Consultation Document by HM Treasury (June 1996), para 35.

[50] For the full definition, see Financial Services Act 1986 (Extension of Scope of Act) Order 1996, above, art 3.

[51] Cf below, para 2.32.

[52] See below, para 2.22.

[53] See below, paras 2.24, 2.25.

is to vest title to securities in a nominee. [54] Finally, investors may hold overseas investments which are dealt with in other markets which employ computerised clearing systems similar to CREST.[55] It may often be convenient for them to use nominees for the conduct of such dealings.

2.13 The employment of nominees in investment matters may "often be seen as best practice", but, as we have indicated above,[56] it is not something that it is open to trustees to do in the absence of express authorisation in the trust instrument. As we explain in Part VII of this Paper, the inability of trustees to employ nominees flows from their obligation to keep trust property under their control.[57] However, although the employment of nominees is now widespread,[58] and it might therefore be thought to be as suitable for trustees as for any other investors, it is acknowledged to be subject to—

> several well-rehearsed disadvantages... The investor's name does not appear on the register, the broker rather than the investor is entitled to receive the company's annual report and accounts and the shareholder perks, and it is the broker that it is entitled to attend and vote at company meetings.[59]

These disadvantages can be reduced in essence to two: risk for the beneficial owner of the investments[60] and exclusion from the rights of shareholding.[61] These are obviously factors that need to be considered in weighing up whether trustees, as fiduciaries, should have default powers to employ nominees and custodians.[62]

Disadvantages

[54] See below, para 2.28. There are two other systems of paperless dematerialised trading in this country. The first is the Central Gilts Office (which has a statutory framework: see the Stock Transfer (Gilt-edged Securities) (CGO Service) Regulations 1985, 1985 SI No 1144). This is "an electronic system for the paperless settlement of gilt-edged securities": see Joanna Benjamin, *The Law of Global Custody* (1996) p 148. Chapter 11 of that book contains a full account of the CGO. Under the CGO system, stock can be registered in nominee accounts: *ibid*, p 151. The second system of dematerialised trading is the Central Moneymarkets Office. This is "a depositary and electronic settlement system for sterling money market bearer securities such as bills and certificates of deposit": *ibid*, p 160. It has no statutory framework. CMO accounts may also be opened by a member in nominee names: *ibid*, p 162. For an account of the CMO, see *ibid*, Chapter 12.

[55] Examples include CEDEL and EURO clear (which are clearing systems for Eurobonds), and American depository receipts. See Joanna Benjamin, *The Law of Global Custody* (1996) Chapter 3.

[56] Para 2.2.

[57] See below, paras 7.2 and following.

[58] It has been estimated that over half the shares by value in this country are held by nominee companies: see Central Statistical Office, Share Ownership: The Share Register Survey Report end 1993, para 3.1.

[59] Dr Brian Ludlow, "CREST Goes Active" (1996) 9 Compliance Monitor 13, 14. See too, M Heneker, "Shares in nominee names" (1995) 139 SJ 531.

[60] See below, para 2.14.

[61] See below, para 2.16.

[62] See below, para 2.17.

RISKS FOR THE BENEFICIAL OWNER

2.14 There are a number of obvious risks to the beneficial owner if the title to his or her investments are vested in a nominee. The principal ones were identified by SIB in 1995 as follows—

(1) misappropriation through forgery and fraud;

(2) wilful or accidental destruction;

(3) theft;

(4) loss in transit;

(5) unauthorised delivery to a third party;

(6) misapplication of one client's investments to satisfy another's obligations;

(7) unauthorised use of a client's investments for the purposes of the nominee or custodian;

(8) failure to maintain proper records which adequately identify a client's entitlement to investments; and

(9) mixing the client's investments with those of the nominee or custodian so as to place them at risk in the event of the insolvency of the nominee or custodian.[63]

2.15 As we have indicated above,[64] the safeguarding and administering of investments - in so far as it is conducted within the United Kingdom[65] - has recently been designated investment business, so that it is regulated by the Financial Services Act 1986.[66] Investors now enjoy the protection of that Act in relation to such custody services, and the SROs also have rules which regulate these activities.[67] The decision to impose regulation was a direct response to the risks outlined in the previous paragraph. The rules of the SROs do in fact have as one of their fundamental principles the proper safeguarding of customer assets.[68] It is also possible for firms offering nominee services to obtain what is known as "default insurance". This guarantees the assets of their customers in the event that the nominee goes out of business. In practice the cost of such insurance is such that it is generally taken out only by the larger firms of brokers.

[63] Custody, Consultative Paper No 90, para 2.1.11.

[64] See para 2.9.

[65] Which will not of course encompass all cases where investors employ nominees.

[66] It should be noted that the safeguarding of valuable items which are not investments are deliberately excluded from regulation under the Financial Services Act 1986: see Custody: A Consultation Document by HM Treasury (June 1996), para 16. It should be noted that the safeguarding and administration of investments is one of the services which may be provided in the United Kingdom by a European investment firm under the Investment Services Regulations 1995, 1995 SI No 3275. For those regulations, see further para 2.19.

[67] See Adrian Butterworth, "Regulating Custody" (1996) 9 Compliance Monitor 78.

[68] See IMRO Rules, r I-1.3(7); SFA Rules, Principles, 7.

LOSS OF SHAREHOLDER RIGHTS

2.16 The second drawback to the use of nominees by investors is in relation to the potential loss of shareholder rights - especially those of corporate governance - and the substance of it has been set out above.[69] A number of attempts have been made to address this issue of which two merit mention here.[70] First, in August 1995, ProShare[71] drew up a voluntary Nominee Code which has two main objectives—

(1) to provide investors with clearer information as to the costs of using nominee services and of the regulatory arrangements that are in place;

(2) to enable investors to protect their rights as shareholders in relation to receipt of information about the company, attendance at general meetings and the receipt of rights issues, scrip dividends and similar benefits.

The Code is applicable only to portfolios managed by investors themselves and not to managed funds. As of October 1996, over 200 companies - but only 4 brokers - had agreed to follow the ProShare Nominee Code,[72] despite the support which it enjoys from HM Treasury.[73] Secondly, in November 1996, the Department of Trade and Industry and HM Treasury issued a joint consultative document, Private Shareholders: Corporate Governance Rights. This explores the possibility of legislation to ensure the rights of investors under nominee schemes of a non-discretionary character[74] to receive company information and any benefits from share ownership, and to participate in corporate governance. The outcome of that consultation is expected later this year.

2.17 Of the two main drawbacks to the employment of nominees, the first has been substantially addressed - through regulation under the Financial Services Act 1986 - and the second is likely to be if, on consultation, it is considered to require legislation. Given the centrality of nomineeship to modern investment practice, we do not in these circumstances regard these drawbacks as a reason for denying trustees the benefit and convenience that can result from employing nominees.

[69] See para 2.13.

[70] See too in relation to personal equity plans, the PEP Regulations 1989 (as amended), 1989 SI No 469.

[71] ProShare is an independent non-profit making organisation set up in 1992 to promote share ownership among individuals and employees: see Department of Trade and Industry and HM Treasury, Private Shareholders: Corporate Governance Rights: A Consultative Document (November 1996), p 30. We are very grateful to ProShare for sending us a copy of the Code.

[72] See "Nominee Investor Scheme" (1996) 5/12 The Company Secretary, 8.

[73] See Custody: A Consultation Document by HM Treasury (June 1996), para 48.

[74] Thereby excluding funds managed on a discretionary basis, managed PEPs, unit trusts, etc: see para 1.1.

The employment of discretionary fund managers

Introduction

2.18 In the absence of any wider powers in the trust instrument, the trustees must select the trust investments themselves,[75] though they will normally do this only after taking professional advice.[76] In managing the investments of the trust therefore, trustees require the services of agents who will provide investment advice and will then execute their instructions. However, it is increasingly difficult for trustees to adhere to this traditional approach that the law presently requires of them. First, some financial services firms either do not offer a discrete advice and execution service at all, or do so exceptionally only for long-standing or particularly valued clients. Secondly, the traditional approach is no longer an effective means of managing trustee investments. If successful investment is to take place, decisions may have to be taken rapidly and it may not be possible to obtain the agreement of the trustees in time.[77] In practice, for any trust that has substantial investments, the employment of a discretionary fund manager is a necessity, a fact that has been judicially recognised.[78] The functions of such a fund manager can be best understood by examining the terms of a typical discretionary fund management agreement.

2.19 We have chosen for this purpose the Terms for Discretionary Fund Management of the Institutional Fund Managers' Association and the London Investment Banking Association ("IFMA Terms").[79] It should be emphasised that these terms have been selected only because they illustrate well the types of conditions that are commonly found in discretionary fund management agreements. We understand that there are in fact no sets of terms that are in anything approaching standard use. The reasons for this are obvious when the range of discretionary arrangements is borne in mind. First, there may be differences between the terms on which business is transacted according to whether the customer is an ordinary business investor or a private customer.[80] The IFMA Terms tend to be used more by the former. Those brokers who generally act for private customers, often have their own terms which are modelled on the SFA or IMRO requirements.[81] Secondly, an investor may wish to invest in a state (other than the United Kingdom) within the European Economic Area. Under the Investment Services Regulations 1995,[82] a European investment firm,[83] which is authorised in the manner specified in those Regulations,[84] is able to provide investment services in this

[75] As we explain below, para 3.3, unless the trust instrument otherwise provides, it is their non-delegable *duty* to do so.

[76] The advice must be considered by the trustees: they must not act at the dictation of their advisers: see below, para 3.6.

[77] See below, para 2.45.

[78] See *Steel v Wellcome Custodian Trustees Ltd* [1988] 1 WLR 167, 174; below, para 2.44.

[79] November 1996 edition. We are very grateful to the Institutional Fund Managers' Association for providing us with a copy of the latest version of the Terms.

[80] Trustees will usually be private customers: see above, para 2.9.

[81] Such terms do however raise very similar points to those found in the IFMA Terms.

[82] SI 1995 No 3275, implementing the Investment Services Directive: Council Directive 93/22/EEC (OJ L141, 10.5.1993, p 27).

[83] Defined by reg 3.

[84] See reg 3.

country, including discretionary fund management.[85] This is so even though it is not authorised under the Financial Services Act 1986, provided that it complies with that Act[86] and meets certain other requirements.[87] Obviously the terms on which they transact business will differ from those of United Kingdom based managers. Thirdly, investors wishing to invest outside the European Economic Area may wish to employ an overseas fund manager directly, rather than acting through an English manager with an overseas associate. That firm will of course transact business on its own usual terms and subject no doubt to its local law. As each of these examples involves the delegation of the power of investment, trustees would not have power to enter into such a management agreement in the absence of some provision in the trust instrument.[88]

A typical discretionary fund management agreement

2.20 Under the IFMA Terms, a discretionary fund manager normally acts as agent for the customer in conducting his or her investment business.[89] However, as we explain in the following paragraphs, it is an agency that is qualified by the express provisions of those Terms.[90]

2.21 So far as are relevant to this Paper, the rights and duties of a discretionary fund manager which contracts with a client under the IFMA Terms are as follows.

(1) It undertakes to manage a fund in accordance with "the investment objectives and any restrictions" specified by the customer in his or her agreement with the manager,[91] to keep those objectives and restrictions under review and to make suggestions from time to time for their amendment.[92]

(2) It undertakes to "act in good faith and with due diligence".[93]

(3) It is given "complete discretion for the account" of the customer together with very wide powers (which may be exercised without prior reference to the client

[85] See Investment Services Regulations 1995, reg 5; and Investment Services Directive, above, Annex A, para 3.

[86] This is the effect of the powers given to SIB by the Investment Services Regulations 1995, reg 9.

[87] See, eg Investment Services Regulations 1995, reg 6.

[88] For the powers of trustees to delegate their trusts, powers and discretions under Trustee Act 1925, s 25, see below, para 3.35.

[89] Cl 5(a). Cf IFMA Terms, cl 14(d).

[90] The extent to which fiduciary duties - such as those of an agent - can be excluded or qualified contractually has been considered in recent years by both the courts and this Commission: see Fiduciary Duties and Regulatory Rules (1995) Law Com No 236. Largely as a result of the decision of the Privy Council in *Kelly v Cooper* [1993] AC 205 (a case concerning an estate agent who had acted for the vendors of two adjacent properties), it is now generally accepted (and we ourselves have concluded) that "the scope of the fiduciary duties owed by an agent to his principal is defined by the express and implied terms of the contract of agency, and that a clear and unambiguous duty defining or exclusion clause will delimit the scope of the fiduciary duties owed to the customer": Fiduciary Duties and Regulatory Rules, above, para 7.3.

[91] IFMA Terms, cl 5(a). This term reflects the requirements imposed upon fund managers by IMRO Rules, r II-2.4(1)(a) and the Appendix to that rule, paras 11 and 12.

[92] IFMA Terms, cl 5(c).

[93] *Ibid*, cl 5(a).

but must be exercised subject to the overriding principles of suitability[94] and best execution[95]) to—

(a) deal in investments and other assets;

(b) make deposits and subscribe to issues, etc; and

(c) take day to day decisions and otherwise act as it judges appropriate in relation to the management of the fund.[96]

(4) It may delegate any of its functions under the agreement to an *associate*.[97] Where reasonable, it may also employ an *agent* to perform "any administrative, dealing or ancillary services required to enable the manager to perform its services" under the agreement.[98]

(5) Both the manager and any associate are empowered to enter into transactions on behalf of their client which may involve a potential conflict of interest,[99] without incurring any liability to account for any profit or other gain made in any other connected transaction.[100] However, the manager must ensure that any such transaction is effected on terms which are not materially less favourable to the client than if the conflict had not existed.[101]

(6) Although the manager normally acts as agent, there are occasions when it may deal as principal. To enable both it or its associate to do this, the agreement provides that the services which either of them provide under the agreement do not give rise to any "fiduciary or equitable duties" such as would hinder them in so acting.[102]

(7) The manager is responsible for any loss to the client only to the extent that it is due to "the negligence, wilful default or fraud" of itself, any associate to

[94] For the obligation on a fund manager to ensure the suitability of personal recommendations and discretionary transactions, see IMRO Rules, r II-3.1.

[95] IFMA Terms, cl 1, defines "Best Execution" as "the method whereby an investment manager seeks to achieve the best terms for a customer". The obligation derives from IMRO Rules, r II-3.8.

[96] IFMA Terms, cl 5(a).

[97] *Ibid*, cl 6(a). An associate is a company or other person connected to the fund manager, or the custodian who provides custody services to the fund. The sort of case that is likely to arise is where the fund manager wishes to invest part of the fund abroad and entrusts the management of that part to a connected firm in that foreign state. This clause does of course empower the delegation of the manager's *discretionary* powers and is not confined to its ministerial acts.

[98] IFMA Terms, cl 6(b). In selecting and controlling an agent, the manager undertakes to act "in good faith and with due diligence": *ibid*. There is no power under this clause to sub-delegate *discretions* to an agent, but only ministerial acts.

[99] To meet the requirements of IMRO Rules, r II-3.3(1), IFMA Terms, cl 14(c) gives examples of the kind of conflicts which may arise, as where the manager undertakes investment business for another client, or has some interest in a company whose securities are held or dealt with on behalf of the client.

[100] IFMA Terms, cl 14(a).

[101] *Ibid*, cl 14(b).

[102] *Ibid*, cl 14(d).

whom it has delegated its functions under (4), above, or any employee of the manager or the associate.[103]

2.22 In practice, it is usual for an investor who employs a fund manager to vest his or her securities in a nominee (referred to in the IFMA Terms as "the Custodian") to facilitate dealings. The nominee, who may or may not be the fund manager,[104] will usually be responsible for the safekeeping of the investor's securities, settling transactions made by the manager, collecting income on behalf of the investor and carrying out any other administrative acts in relation to the fund.[105]

2.23 These terms pose a serious problem for trustees who wish to employ the services of a discretionary fund manager.[106] First, under the IFMA Terms, the client "warrants that it has full power to employ the Manager... on the terms of the Agreement".[107] As we explain more fully later in this Paper,[108] a trustee would *not* have power to enter into an agreement with a discretionary fund manager on these terms in the absence of a wide authority in the trust deed, and would therefore be in breach of trust if he or she did so.[109] To be adequate, any such express authority would have to empower the trustee both to delegate his or her fiduciary obligations as to investment *and* to allow the agent to sub-delegate those obligations. Secondly, as we explain in Part VII of this Paper, trustees cannot place trust assets in the hands of a nominee in the absence of authority in the trust instrument. One apparent obstacle to the employment of a discretionary fund manager that emerges from the IFMA Terms is not in practice a real barrier. We have noted that the IFMA Terms exclude the normal rules which prohibit an agent from profiting from his or her fiduciary position and from placing him or herself in a position where fiduciary duty and personal interest conflict.[110] We explain later in this Paper[111] that there is some doubt whether trustees can authorise their agents to contract on the basis that they can engage in conduct which the trustees themselves could not.[112] However, although a provision of this kind is not uncommon in discretionary fund management agreements,[113] we understand there are brokers who are perfectly willing to contract on terms that they will *not* conduct themselves in such a way as to lead to conflicts of interest.[114]

[103] *Ibid*, cl 18.

[104] Where an outside custodian is appointed, the IFMA Terms require the investor to ensure that it is willing and able to accept instructions from the fund manager: cl 28.

[105] Cf IFMA Terms, cl C1 (which applies where the nominee is a party to the agreement).

[106] See the valuable discussion by Andrew Mortimer, "Trustees and Investment Management: Part I" [1994] Private Client Business 109; "Trustees and Investment Management: Part II", *ibid*, 160.

[107] Cl 19(a).

[108] Below, paras 3.20 and 5.3.

[109] In the Explanatory Notes to the IFMA Terms, there is a warning that "if you are entering into the agreement in your capacity as trustee... you should seek advice to confirm that you have power to enter it generally and on the terms proposed".

[110] See above, para 2.21(5).

[111] Below, para 3.26.

[112] See Andrew Mortimer, "Trustees and Investment Management: Part II", above, at p 163.

[113] We have, for example, seen an agreement made with a trust (not under the IFMA Terms) which contained such a clause.

[114] We are very grateful to APCIMS for this point.

CREST

The legal background

2.24 The Companies Act 1989 authorised the Secretary of State to make regulations "for enabling title to securities to be evidenced and transferred without a written instrument".[115] The purpose of this section was to provide a legal framework within which the Stock Exchange could introduce a system for the holding of shares in dematerialised form and for transactions to be effected electronically. Although the scheme that was visualised in 1989[116] had to be abandoned in 1993, there is now in place another system called CREST.[117] This operates in accordance with the Uncertificated Securities Regulations 1995,[118] which were made under the powers conferred by the Companies Act 1989. CREST has now replaced the previous Talisman settlement system, which had been in operation for eighteen years. A brief account of how CREST works is necessary to understand its legal implications for trustees.[119]

What is CREST?

2.25 CREST is a computer-based system[120] for the electronic transfer of and settlement of trades in securities.[121] It is at present confined to the settlement[122] of ordinary shares, preference shares, warrants, corporate loan stocks and debentures[123] which are registered in either the United Kingdom, the Irish Republic or the Isle of Man.[124] The purpose of the system is to enable securities "to be evidenced otherwise than by a certificate and transferred otherwise than by a written instrument".[125] It replaces the former paper-based system of shareholding and transfer with an electronic book entry system. Payment facilities are provided by a number of specified payment banks.[126]

[115] Section 207(1). For the power to make regulations, see *ibid*, s 207(9). Section 207 lays down the necessary framework for such regulations.

[116] Known as "Taurus".

[117] We are very grateful to Crest Co Ltd for kindly providing us with a great deal of material on the operation of CREST.

[118] SI 1995 No 3272.

[119] This account is limited only to matters germane to this paper. For a fuller treatment, see Joanna Benjamin, *The Law of Global Custody* (1996) Chapter 13. For shorter discussions of CREST, see Charles Marquand, "CREST and the shareholder" (1996) 140 SJ 668; Dr Brian Ludlow, "CREST goes active" (1996) 9 Compliance Monitor 13.

[120] See Uncertificated Securities Regulations 1995, above, reg 2(1).

[121] *Ibid*, reg 3(1), which defines "securities" for these purposes. The Regulations refer to dealings in "units of security". Such a unit is defined to mean "the smallest possible transferable unit of the security (for example a single share)": *ibid*.

[122] That is, the actual delivery of securities against payment of the price. The buying and selling of shares remains a matter for the Stock Exchange.

[123] This is considerably narrower than the range of "securities" listed in reg 3(1). CREST cannot yet be used to settle trades in gilts, bonds or unit trusts, all of which are included in that definition. For the first debenture issue to come to CREST, see (1997) 94/10 LSGaz 9.

[124] The legal framework in the Uncertificated Securities Regulations 1995, above, obviously applies only to the United Kingdom, but equivalent regulations have been made in Ireland and the Isle of Man.

[125] Uncertificated Securities Regulations 1995, reg 2(1).

[126] Of which there are currently 13 which settle in pounds sterling and 7 which settle in Irish punts.

The Operator is CREST Co Ltd.[127] Although securities may be held in "uncertificated" paperless form, there is at present no requirement that they must be. Those who wish to retain their securities in "certificated" form may do so. Indeed the Operator is required to have a system which enables members[128] to change the form in which they hold securities from certificated to uncertificated or *vice versa*.[129]

Electronic settlement

2.26 CREST enables trades of securities to be settled electronically. Those who settle in this way are called "CREST members".[130] They are permitted by the Operator to send properly authenticated instructions[131] via the computer system. [132] Those CREST members who are also "users",[133] may send and receive properly authenticated computer instructions[134] not merely on their own account but on behalf of other persons, who are known as "sponsored members".[135] Subject to certain limited exceptions, the sending[136] of dematerialised instructions relating to an investment on behalf of another is now an activity that amounts to the conduct of investment business for the purposes of the Financial Services Act 1986.[137] This provides additional protection for investors because it means that users[138] must be authorised under that Act.

Using CREST: contractual obligations

2.27 It is unnecessary to examine in any detail the contractual obligations that a member must undertake under the terms of the CREST Membership Agreement. What is relevant for present purposes is the position of a sponsored member.[139] He or she must appoint both—

(1) a sponsor, which will be a user and will therefore be able to input instructions to the computer system on behalf of the sponsored member; and

[127] For the regulation of the Operator, see Uncertificated Securities Regulations 1995, Part II and Sched 1.

[128] For "sponsored members", see below, para 2.26.

[129] Uncertificated Securities Regulations 1995, Sched 1, para 13(a).

[130] Or "system-participants" under the Uncertificated Securities Regulations 1995, reg 3(1).

[131] Called "dematerialised instructions": *ibid*, reg 3(1).

[132] The Operator is required to lay down specifications that must be met to identify the source of a computer instruction as being from the particular system-participant and to minimise fraud and forgery: Uncertificated Securities Regulations 1995, Sched 1, para 5(b).

[133] Known as "sponsoring system-participants" under the Uncertificated Securities Regulations, reg 3(1).

[134] Such as to buy or sell securities.

[135] Or "system-members" under the Uncertificated Securities Regulations 1995, reg 3(1).

[136] Or offering or agreeing to send.

[137] Financial Services Act 1986 (Uncertificated Securities)(Extension of Scope of Act) Order 1996, 1996 SI No 1322, cl 2(1), adding a new para 16A to Financial Services Act 1986, Sched 1, Part II.

[138] Ie, "sponsoring system-participants".

[139] See further, Joanna Benjamin, *The Law of Global Custody* (1996) p 177.

(2) a payment bank, which will provide payment services to the sponsored member.[140]

Although this means that a sponsored member will have to enter into three distinct contracts to enable him or her to take advantage of CREST, namely a CREST Membership Agreement with the Operator, CREST Co Ltd; with a user as sponsor; and with a payment bank, our inquiries suggest that this is not a real problem.[141] Investors are advised to "look for a sponsor who is financially solid and to ensure that he acts only on properly authorised instructions" and to enquire "whether the sponsor has adequate reconciliation procedures and insurance cover against dishonest employees".[142] It may not always be easy, however, to ascertain a user's insurance arrangements.[143]

Uncertificated securities

2.28 Investors have a number of options open to them as to both the form and the manner in which their securities are held. First, they may, as indicated above,[144] retain their securities in certificated form. The drawback with this is that, if they buy or sell certificated securities, the brokerage charges may be higher than they would be if the holdings were dematerialised.[145] Furthermore, although there is no immediate prospect that the holding of securities in certificated form will be phased out,[146] it seems inevitable in time. However, for those who do not trade shares very often, certificated holdings will no doubt remain the norm, at least for the present. Secondly, investors may choose to have their holdings in uncertificated form. They may do this in one of three ways—

(1) They may become CREST members. This is not likely to be common amongst private investors, except for those investing on a large scale, both because of the requirement of having access to the computer system and the costs.

(2) They may become sponsored members. This means that their securities will be registered in their name and they will have the legal title to them. They will therefore receive, as now, the usual information from the company in which they invest, together with any benefits that it offers to, shareholders. As indicated above,[147] to be a sponsored member, an investor will have to enter

[140] See Crest Membership Agreement, cl 3.1; Crest Rules, r 1, para 3.

[141] Brokers do of course offer a package to investors.

[142] See the discussion paper issued by the CREST Project Team at the Bank of England, "CREST: Sponsored Membership of CREST for the Private Investor" (April 1995), Introduction, para 5.

[143] See "Crest and rolling settlement" (1995) 92/20 LSGaz 33, 34 (in the context of brokers, who may act as sponsors). These concerns arose before CREST was operational and may have been unduly pessimistic. From our own inquiries, we are aware that a number of brokers have full insurance cover *and* publish their arrangements.

[144] See para 2.25.

[145] For example, one broker from whom we obtained particulars, adds a fee of £10 per bargain for a certificated transaction.

[146] "[M]any brokers expect to offer efficient paper settlement for the foreseeable future": Department of Trade and Industry and HM Treasury: Private Shareholders: Corporate Governance Rights: A Consultative Document (November 1996), para 2.5.

[147] See para 2.27.

into a CREST Sponsored Membership Agreement and meet the requirements that it imposes, though these are not onerous either in terms of paperwork or expense.[148]

(3) They may vest their securities in a user as a nominee.[149] That user will dematerialise those securities and hold them in uncertificated form on a bare trust for the investor, dealing with them as instructed. We suspect that many discretionary fund managers will become users.

It is worth emphasising that CREST is still in its infancy, and established practices have yet to develop.[150] In particular, until all shares are traded on CREST, it is difficult to assess how popular sponsored membership is likely to be, though we have been told that there is some evidence of a move away from the use of nominees in favour of sponsored membership.

CREST and trustees

2.29 Trustees who wish to use the CREST system will certainly be able to do so, subject to one significant limitation that we explain below.[151] First, it is open to them to continue to hold their securities in certificated form and to deal with them accordingly. As we have explained, this will be more expensive in terms of brokers' fees than if they were held electronically.[152] Furthermore, this option is unlikely to remain available indefinitely.[153]

2.30 Secondly, the Uncertificated Securities Regulations 1995 specifically authorise trustees to become sponsored members of CREST[154] in the absence of an express prohibition on them doing so.[155] They will not be liable for breach of trust by reason only of their becoming such a member. There is no reason why trustees should not become sponsored members. Although CREST has not been in operation long enough to obtain an accurate picture, our limited inquiries have revealed that sponsored membership is not expensive,[156] and presents few (if any) problems in practice.

[148] See below, para 2.30.

[149] It may not be the user itself that is a nominee, but a connected nominee company.

[150] In the Chief Executive's Review in CREST Co Ltd's Annual report for 1996 (which takes into account developments up to the end of March 1997), it is stated that "[t]he take-up of sponsored membership by private individuals is low, at 250. We expect to see growth in this during 1997, now that investors can dematerialise their entire portfolio in one process, stimulated by continuing interest from firms which are offering this facility to their clients": p 7.

[151] See para 2.31.

[152] See above, para 2.28.

[153] Even if the legal framework continues to permit certificated holdings, it is conceivable that brokers may refuse to deal in them.

[154] Ie, "system members" under those Regulations.

[155] Reg 33(1)(*c*). The regulation does not specify that the express prohibition has to be in the trust instrument. If the trustee were a professional, it could presumably be contained in any contract made with him or her.

[156] "As far as sponsored membership is concerned, a number of brokers are offering the service with charges ranging from nothing to £100 per year": Dr Brian Ludlow, "Crest Goes Active" (1996) 9 Compliance Monitor 13, 14. Of the two brokers offering sponsored membership that we contacted, one made no charge and the other charged only the CREST Co membership fee of £20.

2.31 Thirdly, trustees may wish to adopt the course that many private investors will probably follow and vest their securities in a user as nominee. However, in the absence of authority in the trust deed - and few but the most recent trust deeds confer such authority[157] - trustees have no power to place trust assets into the hands of nominees. If they do so, they risk incurring liability for breach of trust should any loss to the trust ensue.[158] It follows therefore, that in this one respect, trustees will be at a disadvantage as against other private investors.

Five-day rolling settlement

2.32 As part of a programme to improve the system by which shares are paid for and transferred, a system of rolling settlement was introduced by the London Stock Exchange in July 1994. Formerly, payment for and transfer of shares occurred on fortnightly account days, when two weeks' business was settled on one day. By contrast, under rolling settlement, settlement takes place every working day because shares are transferred and paid for a specified number of days after the trade.[159] When the new system was introduced, settlement took place ten days after the trade - ten-day rolling settlement. However, in June 1995, the period was reduced to five days, to bring United Kingdom practice into line with common international practice. It is visualised that it will be reduced to three days in due course.[160]

2.33 The expedition of the process of settlement does of course create certain obvious practical problems. First, a broker who is selling shares in certificated form will need to have in advance both the transfer forms signed by the seller, and the share certificates.[161] Secondly, intending buyers must ensure that funds are available to the broker to pay for the shares. It may not always be practicable for those wishing to sell shares very quickly to have the necessary paperwork completed in time. In the light of these difficulties, it is not surprising that, to facilitate the sale of shares, it has become normal for brokers to offer both nominee and banking services. To assist sales, the shares can be held by a nominee company on a bare trust for the shareholder and can be transferred by the company at his or her direction. To facilitate purchases, the broker can offer credit.

2.34 Where the shares are held by trustees in certificated form,[162] five-day rolling settlement poses a particular practical difficulty. It will be necessary to obtain the signatures of all the trustees in order to sell the shares. This inevitably takes time and means that it will

[157] See above, para 1.11.

[158] See below, para 7.3.

[159] Rolling settlement applies to dealings in shares both when they are held in certificated form and when they are dematerialised.

[160] Cf Joanna Benjamin, *The Law of Global Custody* (1996) pp 171, 172.

[161] The position is different where the securities are held in dematerialised form. The basis on which brokers will accept instructions from trustees is a matter of contract between the parties. We understand that, even within one firm of brokers, it may vary from client to client. At one extreme, all the trustees may have to give their prior consent in writing. More usual is an arrangement by which one of the trustees has authority to act on behalf of all of them. He or she may give instructions either by fax or by telephone to the broker and in the latter case will either use a password, or will be known to the person with whom he or she deals.

[162] No equivalent difficulty arises where securities are held in dematerialised form. As we have indicated in the previous footnote, trustees make their own contractual arrangements for dealing in such securities which may allow for expeditious dealing.

not often be possible to arrange a sale of trust shares quickly, in order to take advantage of opportune conditions.[163] In the case of a trust with a large shareholding, the volume of sales may be considerable and the consequent paperwork substantial. However, as we have already noted[164] and for reasons that we explain more fully in Part VII,[165] the law at present precludes trustees from vesting trust shares in a broker's nominee company unless expressly authorised by the trust instrument. Although non-standard settlement periods can at present be negotiated (which might enable trustees to overcome some of these difficulties), this arrangement is not likely to continue beyond the short term and the costs may, in any event, make it unattractive.[166]

LAND HOLDINGS

Introduction

2.35 Trustees may, if authorised, hold land as an investment.[167] For the purposes of exercising their functions as trustees, trustees of land have in relation to the land held in trust all the powers of an absolute owner,[168] unless provision is made to the contrary in the disposition creating the trust.[169] Many of their powers of dealing with the land, such as powers of sale, leasing and mortgaging, are fiduciary powers, which under the existing law, cannot be delegated without express authority in the trust instrument.[170] There are a number of aspects of the holding and management of such land of which we are aware that are relevant to the issues considered in this Paper. We single out three specific examples, but there are no doubt others where the present law may inhibit the most effective administration of trusts with land holdings and we would be glad to hear of them from readers.

Vesting title in nominees

2.36 First, it may be convenient for the title to the land to be vested in a nominee. This is particularly so where the title to the land is registered. Should the trustees change - and in some trusts they change fairly regularly - it will then be unnecessary to register the change of trustee at the Land Registry.[171] Because of the rule that trustees must retain the ownership of trust assets, this practice cannot at present be adopted in the absence of express authorisation in the trust deed.

Delegation of estate management

2.37 Secondly, where the trust consists of land holdings, the trustees may wish to delegate

[163] Cf para 2.45, below.

[164] See above, para 2.2.

[165] See below, para 7.3.

[166] See "Crest and rolling settlement" (1995) 92/20 LSGaz 33.

[167] For the circumstances in which trustees may invest in land and our proposals in relation to their powers, see Part VIII of this Paper.

[168] Trusts of Land and Appointment of Trustees Act 1996, s 3(1). The Act came into force on 1 January 1997 (for the Commencement Order, see SI 1996 No 2974), but applies to most existing trusts of land other than Settled Land Act settlements: *ibid*, s 1.

[169] *Ibid*, s 8(1).

[170] See below, para 3.3.

[171] Where title is unregistered, the deed of appointment automatically vests the title to the land in the new trustee without more: Trustee Act 1925, s 40.

the management of the land to an agent. At one level, this may involve no more than the employment of a farm manager, something which the trustees will of necessity have to do. However, it is possible to envisage cases where the trust has substantial holdings of rented property, something that may indeed become a commonplace once again following the deregulation of both the private rented and agricultural sectors.[172]

2.38 It has been accepted for many years that trustees can delegate the collection of rents and the day-to-day management of rented properties. There is some authority that suggests that they can also delegate the selection of new tenants when properties fall vacant.[173] This is so, even though the power of leasing is, as we explain, a fiduciary power, that ought therefore to be non-delegable.[174] However, despite this latitude, it seems very doubtful whether, in the absence of express powers in the trust instrument, trustees could delegate to an agent the choice of properties to be purchased for letting.[175] To do so would contravene the rule that the choice of investments is a non-delegable obligation of the trustees alone.[176] We doubt that trustees' inability to make a general delegation of their powers in this context creates anything like the same difficulties as it does in relation to the purchase of securities. However, we shall be interested to learn whether this point has caused any practical difficulty, particularly in relation to any larger trusts.

Rent reviews and sales at valuation

2.39 The third issue concerns rent review clauses in leases and sales of property at a valuation. A trust may either already hold land on trust or the trustees may choose to invest in the purchase of land for letting. Indeed trustee investment in land is likely to become common once again with the deregulation of both the private rented sector by the Housing Act 1988[177] and the agricultural sector by the Agricultural Tenancies Act 1995.[178] Rent review clauses have of course long been the norm in relation to business lettings. They are now sometimes employed in lettings of dwellings,[179] and the Agricultural Tenancies Act 1995 contains a statutory mechanism for rent reviews

[172] By the Housing Act 1988 and the Agricultural Tenancies Act 1995, respectively.

[173] See *Re Muffett* (1887) 56 LJCh 600; below, para 3.11.

[174] See *Robson v Flight* (1865) 4 De G J & S 608, 614; 46 ER 1054, 1057; below, para 3.3.

[175] Each trustee could *individually* delegate his or her power to purchase investments to an agent by means of a power of attorney under the Trustee Act 1925, s 25 (as substituted): see below, para 3.35.

[176] See below, para 3.3.

[177] See the further deregulation of this sector by the Housing Act 1996, ss 96 - 104.

[178] We are aware that, in certain parts of the country, properties are now regularly purchased for investment. Indeed there are organisations, including the Association of Resident Letting Agents (ARLA) that promote such investment (ARLA runs a successful "Buy-to-Let" scheme). The properties are managed by a management company or agent for the owner, and are then let on assured tenancies. There is evidence that this form of investment may provide a good return on capital: see Alan Collett and Chris Phillips, "Landlords go Househunting" [1997] 20 EG 144. Although we have no direct evidence that trusts are investing in land in this way, we think it likely that they will do so particularly if the wider powers for trustees to purchase land which we propose in Part VIII of this Paper were to be introduced.

[179] The use of rent review clauses in relation to assured periodic tenancies is sanctioned by the Housing Act 1988, s 13(5).

which will apply unless the parties contract out of its provisions.[180] If there is a rent review clause, it is inevitable that, if the parties cannot themselves agree a new rent, it will fall to be determined by a third party acting as either an expert or an arbitrator. Quite apart from the leasing of land, trustees may find it convenient to enter into option agreements to sell trust property at a price to be determined at the time when the option comes to be exercised. Usually, the sale will be at a valuation to be made by some independent third party.

2.40 As the authorities stand, there is a difficulty for trustees in relation to both rent review clauses and agreements to sell at a valuation.[181] It arises from two decisions on sales at valuations by trustees and life tenants.[182] Those cases established that it would be a breach of trust for a trustee (and presumably other persons having fiduciary powers) "to delegate his authority and enter into an agreement to sell for a price to be fixed by somebody else".[183] At the time of those decisions, valuation was not undertaken according to any established principles but was impressionistic. There was necessarily an element of discretion in making any valuation and the choice of a given valuer was therefore of considerable importance.[184] If these authorities still hold good, trustees are necessarily precluded from granting either leases containing rent review clauses or options to sell trust property at a valuation. The highly inconvenient consequences of this conclusion are obvious.

2.41 There are at least two reasons for doubting whether these cases still represent the law.[185] The first is that the process of valuation is no longer regarded as a matter for the subjective discretion of the valuer. "Value" is now perceived as something that is objectively ascertainable by valuers according to well understood principles.[186] If trustees refer an issue of valuation to a valuer, they can no longer be said to be delegating a discretion.[187] Secondly, trustees are of course under a duty to obtain the best price or rent that is reasonably obtainable for any property which they sell or let. Given the fluctuations in property prices and rents over recent decades (both upwards and downwards), it is difficult to see how trustees can comply with this duty if they can

[180] See Part II of the Act. As regards agricultural holdings granted before September 1995, see the provisions for the arbitration of rent in the Agricultural Holdings Act 1986, s 12.

[181] See Gavin Lightman QC, "Sales at Valuation by Fiduciaries" [1985] Conv 44. We are very grateful to Sir Gavin Lightman for drawing our attention to this point.

[182] See *Peters v Lewes and East Grinstead Railway Co* (1880) 16 ChD 703 (Hall V-C); 18 ChD 429 (CA); and *Re Earl of Wilton's Settled Estates* [1907] 1 Ch 50. A life tenant is of course a trustee of his or her powers: see Settled Land Act 1925, s 107.

[183] *Re Earl of Wilton's Settled Estates*, above, at p 55, *per* Warrington J.

[184] See Gavin Lightman QC, "Sales at Valuation by Fiduciaries" [1985] Conv 44, 47. This is reflected in the rule that prevailed until *Sudbrook Trading Estate Ltd v Eggleton* [1983] 1 AC 444, that, where the parties provided machinery for valuation that for some reason failed, the court would not substitute its own. In *Sudbrook*, Lord Fraser pointed out that while the means of ascertaining the value might have been an essential part of the agreement between the parties in the early nineteenth century, this was "because the valuer's profession and the rules of valuation were less well established than they are now": [1983] 1 AC at 483.

[185] *Re Earl of Wilton's Settled Estates*, above, has been described as "dubious": see *Emmet on Title* (19th ed 1986) § 2.122.

[186] See *Sudbrook Trading Estate Ltd v Eggleton*, above, at p 479.

[187] See Gavin Lightman QC, "Sales at Valuation by Fiduciaries" [1985] Conv 44.

only grant options or let property at fixed sums.[188] However, despite the doubts as to the continued existence of the prohibition on trustees selling or letting at a valuation, the rule continues to be asserted, albeit without enthusiasm, by a number of leading texts.[189] It is obviously undesirable that there should be any possible doubt as to a matter so basic and important to the proper management of a trust. We shall be interested to learn whether this uncertainty is regarded as a difficulty and whether it does in practice inhibit trustees from entering into transactions in which the price or rent might have to be determined by valuation.

JUDICIAL ATTITUDES TO APPLICATIONS FOR ADDITIONAL POWERS

2.42 Where trustees consider that their powers of management and administration are inadequate, they may apply to the court for their extension.[190] The court will grant them further powers if it considers it to be expedient.[191] There were in fact three reported decisions between 1983 and 1991, each involving a large trust fund, in which an application was made for additional investment powers, and where the trustees also sought wider delegation powers.[192] In each case the powers were granted. The three decisions do of course pre-date the developments in relation to investment in securities that have been outlined above.[193]

2.43 In *Trustees of the British Museum v Attorney-General*,[194] it was proposed that the trustees should have power to employ professional investment managers and to delegate to them the exercise of their powers of investment for a period of up to one year at a time.[195] Any delegation could by revoked or altered at any time by the trustees and the managers were bound to exercise their powers in accordance with the trustees' instructions as to investment policy. The power of delegation was considered to be "plainly advantageous" - even in 1983 - because there were "changed conditions of investment, conditions which require great liberty of choice if, upon skilled advice, advantage is to be taken of opportunities which often present themselves upon short notice and for short periods".[196]

2.44 In *Steel v Wellcome Custodian Trustees Ltd*,[197] trustees were again given authority to

[188] See *Emmet on Title* (19th ed 1986) § 2.122.

[189] See, eg *Emmet on Title* (19th ed 1986) §§ 2.122, 15.005, 22.116; *Halsbury's Laws of England* (4th ed 1983) vol 42, paras 94 and 827.

[190] Applications are normally now made under the Trustee Act 1925, s 57 rather than under the Variation of Trusts Act 1958, for reasons explained in *Anker-Petersen v Anker-Petersen*, briefly reported at (1991) 88/16 LSGaz 32, transcript pp 5 - 9. In the case of charitable trusts, the trustees may apply to the Charity Commissioners rather than to court: see below, para 3.41.

[191] Trustee Act 1925, s 57. See David J Hayton, *Underhill and Hayton: Law of Trusts and Trustees* (15th ed 1995) pp 496 - 497.

[192] *Trustees of the British Museum v Attorney-General* [1984] 1 WLR 418 (charitable trust with capital of more than £5 million); *Steel v Wellcome Custodian Trustees Ltd* [1988] 1 WLR 167 (charitable trust with capital of an astonishing £3.2 billion); *Anker-Petersen v Anker-Petersen*, above (family trust with capital of £4 million). In the *Anker-Petersen* case, the applicant was the life tenant rather than the trustees. The powers of delegation sought were similar in each of the cases.

[193] Paras 2.8, and 2.12 - 2.34.

[194] [1984] 1 WLR 418.

[195] Cf Trustee Act 1925, s 25 (as substituted): see below, para 3.35.

[196] [1984] 1 WLR 418, 424, *per* Megarry V-C.

[197] [1988] 1 WLR 167.

delegate the power of investment to professional advisers for up to a year at a time. Under the scheme approved, the trustees were liable to take reasonable care both in the appointment and the supervision of their agents.[198] Hoffmann J considered that it was inevitable that "day to day investment decisions concerning a fund of this size would have to be delegated to advisers".[199]

2.45 Finally, in *Anker-Petersen v Anker-Petersen*,[200] the court authorised the appointment of a discretionary fund manager and the delegation to him by the trustees of their powers of investment. The arrangements were subject to annual review, investment was to be in accordance with policy guidelines prepared by the trustees, and the trustees were to exercise reasonable care in choosing and supervising the manager. There was also a power for investments to be held by a nominee. In granting the powers the court was influenced both by the size of the fund and by the fact that three of the four trustees lived abroad.[201] This meant that day-to-day consultation was not practicable when it came to "taking those rapid decisions as to buying and selling a particular investment which are sometimes necessary if good opportunities are not to be lost".[202] The power to place trust securities in the name of a nominee was regarded as "merely ancillary to the powers of investment". It was "obviously desirable".[203]

2.46 What these cases demonstrate is that, even before the most recent developments in investment practice, there was a judicial willingness to extend the powers of trustees so that they could delegate their powers of investment to a discretionary fund manager. The cases were unusual in the substantial size of the funds that were held in trust. However, fund management is now much more widely used even than it was in 1990 when the *Anker-Petersen* case was decided. In any event, it was only *because* the trust funds were large, that the gains to be achieved from an application to the court for additional powers could justify the cost. Indeed the cost of an application to the court for additional powers have been estimated to be "not much less than £10,000".[204]

[198] Which is, on the authorities, a higher duty than is applicable under the general law to trustees. See Part IV of this Paper.

[199] [1988] 1 WLR 167 at 174.

[200] December 6, 1990, Judge Paul Baker, QC. There is, inexplicably, no full report of this important case, but only a summary at (1991) 88/16 LSGaz 32. The comments here are based on the transcript.

[201] One lived in Denmark and two in the Isle of Man.

[202] Transcript, p 12, *per* Judge Paul Baker, QC.

[203] Transcript, p 13, *per* Judge Paul Baker, QC.

[204] Deregulation (Trustee Investments) Order 1997, Explanatory Memorandum by HM Treasury, para 28 (relying upon information provided by one branch of the Society of Trust and Estate Practitioners).

PART III
TRUSTEES' POWERS OF DELEGATION - THE PRESENT LAW

INTRODUCTION

3.1 In this Part we examine the circumstances in which trustees[1] may collectively delegate certain of their functions to an agent in the absence of any express power in the trust instrument. We explain what powers of delegation trustees had at common law and how they have been subsequently extended and altered by statute. We examine in turn two particular issues—

(1) the functions which they are permitted to delegate; and

(2) the circumstances in which trustees may delegate.

THE FUNCTIONS THAT MAY BE DELEGATED

The underlying principle: delegatus non potest delegare

3.2 The fundamental rule was stated authoritatively in the leading nineteenth century text on powers, *Sugden on Powers*, as follows—

> whenever a power is given..., if the power repose a personal trust and confidence in the donee of it, to exercise his own judgment and discretion, he cannot refer the power to the execution of another, for *delegatus non potest delegare*.[2]

By reposing trust in a person, the testator or settlor expects that trustee to carry out those responsibilities personally.[3] In *Turner v Corney*,[4] Lord Langdale MR observed that—

> trustees who take on themselves the management of property for the benefit of others have no right to shift their duty on other persons; and if they employ an agent, they remain subject to responsibility towards their *cestuis que trust*, for whom they have undertaken the duty.[5]

[1] Who, for the purposes of this Paper, include personal representatives: cf Trustee Act 1925, s 68(17).

[2] (8th ed 1861) p 179 (the author had by then become Lord St Leonards). See too C J W Farwell and F K Archer, *Farwell on Powers* (3rd ed 1916) p 499: "[a] power involving the exercise of personal discretion by the donee cannot be delegated".

[3] See *Robson v Flight* (1865) 4 De G J & S 608, 613; 46 ER 1054, 1056, where Lord Westbury LC observed that "[s]uch trusts and powers are supposed to have been committed by the testator to the trustees he appoints by reason of his personal confidence in their discretion, and it would be wrong to permit them to be exercised by [another]".

[4] (1841) 5 Beav 515, 517; 49 ER 677, 678.

[5] See too *Speight v Gaunt* (1883) 22 ChD 727, 756 (CA), where Lindley LJ observed that "[a] trustee has no business to cast upon brokers or solicitors or anybody else the duty of performing those trusts and exercising that judgment and discretion which he is bound to perform and exercise himself".

This rule that "a person who has a discretionary power cannot delegate the execution of that power"[6] applies to other fiduciary relationships.[7] Any proposals to relax that rule in relation to trustees and personal representatives must therefore be viewed in that wider context.

No delegation of discretions

3.3 It is important to understand what the rule against delegation does and does not do. In the absence of express authority in the trust instrument or will,[8] it prohibits the delegation by trustees and personal representatives not of all their functions but only of their dispositive duties to distribute the trust property to those entitled to it under the trust,[9] and of their fiduciary discretions,[10] such as the selection of trust investments,[11] or the decision whether or not to sell or lease trust property.[12] It is a breach of trust for trustees to delegate such discretionary functions and they are liable for any consequent loss.[13] This prohibition on the delegation of their fiduciary powers does not however preclude the delegation by them of "powers to do acts merely ministerial".[14]

3.4 Although this distinction between fiduciary powers and ministerial acts is easily stated, the dividing line between those functions which only a trustee may perform and those which may be delegated is not easily drawn.[15] The dividing line has not been the subject of much discussion in English cases save in fairly general terms.[16] There have however been attempts to define the boundary in the United States of America. The traditional view, found in the American *Restatement of Trusts, Second*,[17] was that the following factors were relevant in determining whether a function was one which

6 *Re Airey* [1897] 1 Ch 164, 170, *per* Kekewich J. See too *Re Parry, decd* [1969] 1 WLR 614, 618, where in relation to a trustee, Pennycuick J spoke of "the exercise of powers and discretions which cannot be delegated to others".

7 Considered below, paras 5.7 and following.

8 "The law is not that trustees cannot delegate: it is that they cannot delegate unless they have authority to do so": *Pilkington v IRC* [1964] AC 612, 639, *per* Viscount Radcliffe.

9 See above, para 1.14.

10 What were described as "powers implying personal discretion": C J W Farwell and F K Archer, *Farwell on Powers* (3rd ed 1916) p 498.

11 See, eg *Rowland v Witherden* (1851) 3 Mac & G 568, 574; 42 ER 379, 381.

12 See on powers of sale: *Clarke v The Royal Panopticon* (1857) 4 Drew 26, 29; 62 ER 10, 12; *Green v Whitehead* [1930] 1 Ch 38 (affirmed on appeal on a different point: (1929) 46 TLR 11); and on powers of leasing: *Robson v Flight* (1865) 4 De G J & S 608, 614; 46 ER 1054, 1056.

13 Thus in *Rowland v Witherden*, above, trustees were held liable where "instead of themselves seeing to the investment of the trust fund, [they] delegated that duty to their solicitor, who misapplied the money": at p 574; 42 ER at 381, *per* Lord Truro LC.

14 C J W Farwell and F K Archer, *Farwell on Powers* (3rd ed 1916) p 498.

15 "It is not always easy to determine whether a particular act is one that it is the duty of the trustee to perform himself and the performance of which it is improper to delegate": W F Fratcher, *Scott on Trusts* (4th ed 1987) § 171.2. See John H Langbein, "Reversing the Nondelegation Rule of Trust-Investment Law" 59 Mo LR 105, 108, 109 (1994).

16 See above, paras 3.2, 3.3.

17 § 171, Comment *d*. The whole approach of *Restatement of Trusts, Third* of 1992 is fundamentally different. It effectively abandons the prohibition on the delegation of discretions and allows the delegation of discretions where a prudent person would do so: see below, para 6.19.

trustees might delegate. These were—

> (1) the amount of discretion involved; (2) the value and character of the property involved; (3) whether the property is principal or income; (4) the proximity or remoteness of the subject matter of the trust; (5) the character of the act as one involving professional skill or facilities possessed or not possessed by the trustee himself.[18]

This analysis has been abandoned in America[19] and in any event, it cannot be assumed that English lawyers would necessarily draw the line in exactly the same way.

The justification for the rule

3.5 It has been said that "[t]he rationale of the nondelegation rule has always been murky".[20] The traditional explanation for it - that trustees cannot delegate their discretions because of the "confidence reposed" in them[21] - is ambiguous. It may mean that the trustees' personal qualities are of importance to the person whose property is held in trust. However, there are many situations where this cannot be so because the trustee or personal representative will be unknown to that person.[22] Alternatively, it may be that confidence is reposed not in the trustee personally, but in the *status* of trusteeship. The obligation on trustees to discharge their duties and discretions personally provides one means of maintaining the high standard of conduct that the law requires of them. A trustee cannot escape liability by delegating to other hands. However, if the rule against the delegation of discretions in its present form is adhered to, the proper management of many trusts is now actually impossible.[23] Far from promoting the more conscientious discharge of the obligations of trusteeship, the rule may therefore force trustees to commit breaches of trust in order to achieve the most effective administration of the trust.[24]

[18] Cited in W F Fratcher, *Scott on Trusts* (4th ed 1987) § 171.2.

[19] The equivalent passage in *Restatement of Trusts, Third*, which lists the factors to be taken into account in considering whether a delegation is proper, § 171, Comment *f*, lists them as: "(1) the nature and degree of discretion involved; (2) the amount of funds or the value and character of the property involved; (3) efficiency, convenience, and cost considerations in light of the situs of the property or activities involved; (4) the relationship of the act or activities involved to the professional skills or facilities possessed by the trustee; and (5) the fairness and appropriateness of the responsibilities in question to the burdens and compensation of the trustee".

[20] John H Langbein, "The Uniform Prudent Investor Act and the Future of Trust Investing" 81 Iowa LR 641, 650 (1996).

[21] *Speight v Gaunt* (1883) 9 App Cas 1, 29, *per* Lord FitzGerald.

[22] This will be the case for example where a person dies intestate because his or her administrator is chosen according to rules of law. Similarly, where a corporate trustee is employed, the settlor is unlikely to know who is in fact administering the trust. Even if the settlor did originally choose a trustee who was known to him or her, that trustee may retire from the trust or die and the new trustee may be someone quite unknown to the settlor.

[23] Cf *Steel v Wellcome Trustees Ltd* [1988] 1 WLR 167, 174.

[24] We have been given examples of practitioners advising trustees to commit breaches of trust because it was in the best interests of the trust that they should do so.

Consultation with beneficiaries

3.6 A trustee, like any other fiduciary, must not act under dictation when exercising his or her discretionary powers.[25] However, trustees do not act under dictation if they merely seek the views of beneficiaries, provided that the ultimate decision as to the exercise or otherwise of the power or discretion is theirs alone.[26] Indeed, such consultation may be highly desirable,[27] and may in certain instances be required by statute.[28] The trustees are, however, fully entitled to reach a decision that is at variance with the wishes of the beneficiaries, provided that they do so in good faith. The court will not override the discretion which the settlor has conferred upon them.[29]

THE CIRCUMSTANCES IN WHICH TRUSTEES MAY DELEGATE

3.7 Even where the function is one that trustees are in principle permitted to delegate, it does not follow that they may always do so. We therefore go on to consider when, in the absence of any express power in the trust instrument or will, trustees may delegate their "ministerial" discretions. We begin by examining the position at common law prior to 1926 before explaining the present law. An explanation of the historical position is essential in order to understand the modern debate as to what the law on trustees' powers of delegation actually is and what it should be.

The position at common law

Legal and moral necessity

3.8 At common law, trustees could not delegate the execution of the trusts at their "own mere will and pleasure"[30] without placing themselves at risk for the acts of their agents. They would be liable for any loss which occurred where they acted "by other hands" except in cases of "legal" or "moral" necessity.[31] The authorities said little about *legal* necessity. It was exemplified by the case where, for some reason, only one of the

[25] *Re Brockbank* [1948] Ch 206, 208; *Holding and Management Ltd v Property Holding and Investment Plc* [1989] 1 WLR 1313, 1324. The actual *decision* in the former of these cases (that where the beneficiaries were all *sui juris* and were together absolutely entitled to the trust fund, they could not compel the trustees to transfer the trust fund to new trustees of the beneficiaries' choosing) has recently been reversed by statute: see Trusts of Land and Appointment of Trustees Act 1996, s 19. However, the *principle* of the case holds good. For the rule against acting under dictation, see P D Finn, *Fiduciary Obligations* (1977) Ch 6. For an extreme case of it, where the trustees did not even appreciate that they were exercising a discretion (a power of advancement), see *Turner v Turner* [1984] Ch 100.

[26] "It would be extremely dangerous to hold that trustees, having such a discretion to exercise, [in that case to retain an investment] might not freely discuss with the beneficiaries the reasons for and against a particular decision, without running the risk of being held to act against their own judgment, if they should disregard, in the end, objections to which they had thought it right in the first instance to direct attention": *Fraser v Murdoch* (1881) 6 App Cas 855, 864 - 865, *per* Lord Selborne LC.

[27] Cf *Re Agricultural Industries Ltd* [1952] 1 All ER 1188, 1190 (liquidator of a company should have consulted contributories).

[28] See, eg Trusts of Land and Appointment of Trustees Act 1996, s 11.

[29] See, eg *Re Steed's Will Trusts* [1960] Ch 407, 418.

[30] *Speight v Gaunt* (1883) 9 App Cas 1, 5, *per* Earl of Selborne LC. For similar reasons, a trustee was not permitted to resign from the trust and assign his trust to another unless authorised by the trust, "because trustees cannot divest themselves of their trust at their pleasure": *Anon* (—) 3 Swans 78n; 36 ER 779, 781.

[31] *Ex p Belchier* (1754) Amb 218, 219; 27 ER 144, 145, *per* Lord Hardwicke LC.

trustees was to receive money payable to the trust.[32] All of the trustees had to sign the discharge because otherwise a good receipt could not be given to the payer.[33] An agent might be employed as a matter of *moral* necessity if to do so accorded with "the usage of mankind". If, according to the ordinary custom of business, it was prudent to employ an agent to carry out a particular task, then the trustees might both employ one[34] and pay him or her.[35] Thus it was, for example, in accordance with such usages to employ a broker to deal in stocks on behalf of the trust,[36] and there was a substantial corpus of authority as to when trustees might delegate some function to solicitors, bankers, auctioneers and other agents.[37] It was also settled that if an agent who had been properly appointed committed some wrongdoing in the course of his employment for which the trustees were held liable by some third party, they were entitled to an indemnity from the trust.[38] It should be noted that if the transaction was inherently imprudent, trustees could not escape from the consequences of their improvidence merely because they employed a competent agent to advise them.[39]

3.9 The doctrine that trustees could delegate only in cases of necessity[40] does not appear to have unduly limited the circumstances in which trustees might employ agents.[41] Most (but not all) of the cases in which trustees were held liable for the defaults of their agents were ones in which the trustees had—

(1) failed to take reasonable care in the choice of their agent;[42]

(2) employed an agent to perform some function that was outside his or her competence;[43] or

[32] To allow this to happen would, in many cases at least, have been a breach of trust. See below, para 3.13.

[33] *Ex p Belchier* (1754) Amb 218, 219; 27 ER 144, 145.

[34] *Ibid*. See too *Joy v Campbell* (1804) 1 Sch & Lef 328, 341, 342; *Clough v Bond* (1838) 3 My & Cr 490, 497; 40 ER 1016, 1018; *Speight v Gaunt* (1883) 22 ChD 727, 742, 756, 763 (CA); 9 App Cas 1, 4, 19 (HL); *Re Gasquoine* [1894] 1 Ch 470, 475, 476, 478.

[35] *Bonithon v Hockmore* (1685) 1 Vern 316; 23 ER 492 (although a trustee who managed the trust estate could not be remunerated for his work on behalf of the trust, he could employ a bailiff and pay him out of the trust fund).

[36] See, eg *Ex p Belchier*, above; *Speight v Gaunt*, above.

[37] For a convenient summary of the law, see H G Hanbury, *Godefroi on the Law of Trusts* (5th ed 1927) pp 200 - 208.

[38] *Benett v Wyndham* (1862) 4 De G F & J 259; 45 ER 1183. In that case a passer-by was injured by a falling bough in the course of tree-felling by reputable woodcutters, employed by the trustees. He obtained judgment against the trustees for his broken leg. They were entitled to be indemnified from the trust fund.

[39] *Learoyd v Whiteley* (1887) 12 App Cas 727 (employment of a valuer did not absolve trustees from liability for the imprudent investment of trust funds in a mortgage of a brickfield).

[40] This represented the law in the United States, though it may now be changing. For the orthodox view, see W F Fratcher, *Scott on Trusts* (4th ed 1987) § 171, where it is stated that a trustee "can properly permit others to perform acts he cannot reasonably be required personally to perform".

[41] Though it was clearly acknowledged that a trustee who employed an agent when there was no need to do so would thereby commit a breach of trust and would have no authority to pay him or her out of trust funds: *Speight v Gaunt* (1883) 9 App Cas 1, 11, 19.

[42] See below, para 4.2.

[43] See below, para 3.12.

(3) failed to exercise proper control over an agent once appointed.[44]

The extent of the doctrine of necessity

3.10 As we have explained above,[45] trustees could not generally delegate their fiduciary powers. Where trustees delegated more than they should, they ran the risk that their conduct might be regarded as "the transferring a trust, which was inconsistent with the duty of a... trustee".[46] However, the courts were not inflexible. In a number of cases, they were prepared to accept that trustees might even delegate certain of their fiduciary powers on grounds of "moral" necessity without them thereby committing a breach of trust. Thus in giving the opinion of the Privy Council in *Stuart v Norton*,[47] the Lord Justice Knight Bruce observed—

> [i]t is said that, according to the English law, a trustee cannot delegate discretion, cannot act by another in a matter of discretion; but even in the English law that general rule may be open to exception...

This point was of particular relevance to English trusts that had to be administered abroad in whole or in part, and Britain's position as a colonial power undoubtedly influenced this pragmatic approach.[48]

3.11 This was not however the only example. First, in *Re Muffett*,[49] the Court of Appeal held that trustees, who had delegated the entire management of some eighty rented properties to agents,[50] were not, as a result, entitled to an annuity given to them under the testator's will for their services. The court did not question the propriety of the delegation despite its extensive nature. Secondly, there is a suggestion in *Speight v Gaunt*[51] that even in making an investment, trustees would be acting properly if they delegated to a broker the choice of the best method of making investments in specified companies, for example, whether to invest in mortgages or in debenture stock. That was considered by Lord Blackburn to be "part of what a stockbroker is generally employed to do".[52] It would obviously be unwise to read too much into these cases, but

[44] See below, para 4.4.

[45] See para 3.2.

[46] *Mathew v Brise* (1845) 15 LJCh 39, 40, *per* Lord Cottenham LC. See too Lord Langdale MR at first instance, *sub nom Matthews v Brise* (1843) 6 Beav 239, 244; 49 ER 817, 819: "Was it not transferring to those persons that trust and confidence for which he was answerable?" In that case, a trustee left Exchequer Bills "to remain undistinguished in the hands of brokers... who held them and had absolute power of disposing of them": *ibid*. The trustee was held liable when the broker misapplied the Bills.

[47] (1860) 14 Moo PC 17, 33; 15 ER 212, 218.

[48] In *Stuart v Norton*, above at p 33; 15 ER at p 218, the Privy Council was "not at the present moment prepared to say, that a trustee in England under an English Will, may not effectually appoint an attorney to act in matters of discretion connected with the trust in a Colony or any Foreign country". The remarks were obiter, because the issue was regulated by the law of British Guiana as the *lex situs* of the land subject to the trust.

[49] (1887) 56 LJCh 600, affirming (1886) 55 LT 671(Chitty J).

[50] The agents were employed by the trustees "to collect the rents, manage the property, inspect and give orders for necessary repairs, to see to the proper completion of such repairs, and to let the property as it becomes vacant": see 55 LT 671, 672.

[51] (1883) 9 App Cas 1, 22.

[52] *Ibid*.

they do suggest not only that the rule against delegating discretions was viewed pragmatically, but that had statute not intervened, the doctrine of necessity might have been developed to allow the delegation of fiduciary discretions in appropriate circumstances.

3.12 One point that did emerge from the authorities was that there could never be any "necessity" to employ persons as agents for tasks that were outside their competence. In *Fry v Tapson*,[53] Kay J explained that—

> [i]f a trustee employs an agent to do that which is not the ordinary business of such an agent, and he performs the unusual duty improperly, and loss is thereby occasioned, the trustee would not be exonerated.

Applications of this principle were not uncommon. For example, trustees were held liable for employing a London surveyor to value land in Liverpool for a mortgage investment,[54] for delegating to a solicitor the selection of a valuer,[55] and for allowing a solicitor to receive trust money.[56]

3.13 The selection of agents was a matter that had to be undertaken by all the trustees collectively. They could not delegate the task to one (or presumably some) of their number.[57] Nor could they entrust the receipt of capital money to just one of the trustees.[58] Payment had to be to all of them or into their joint bank account.[59] Trustees could not expressly authorise an agent to receive the sum,[60] except in cases of moral necessity, as where the trustees were abroad.[61] These limitations caused some inconvenience, especially in conveyancing transactions.[62]

Delegation by trustees to one of themselves

3.14 A question that caused some difficulty was the extent to which trustees might delegate

[53] (1884) 28 ChD 268, 280.

[54] *Fry v Tapson*, above. See too *Budge v Gummow* (1872) LR 7 Ch App 719, where trustees were held liable in similar circumstances, having employed a London surveyor to value land in Broadstairs.

[55] *Fry v Tapson*, above, at p 281.

[56] *Re Dewar* (1885) 54 LJCh 830. A solicitor was employed by trustees to receive the proceeds of sale of a testator's estate which he misappropriated. Kay J asked rhetorically, "has it ever been held that it is a part of the ordinary business of a solicitor to receive trust money?": p 832. He considered that a trustee who did so was "just as much liable as if he put the money in his own pocket": *ibid*. In the Irish case of *Ex p Townsend* (1828) 1 Moll 139, 140, Hart LC explained the matter in terms of moral necessity, observing that "although there is necessity to employ an Attorney, there is no necessity to permit him to receive more than a shilling of the money recovered, further than his costs". See too *Rowland v Witherden* (1851) 3 Mac & G 568; 42 ER 379 (trustees liable for entrusting trust money to a solicitor to invest in a mortgage, but which he misapplied instead).

[57] *Robinson v Harkin* [1896] 2 Ch 415.

[58] The position was different in relation to the receipt of rents from land or dividends on stocks: see below, para 3.14.

[59] *Re Bellamy and Metropolitan Board of Works* (1883) 24 ChD 387.

[60] *Ibid*, at p 400 (Cotton LJ). But see the comments of Baggallay LJ at p 397.

[61] *Ibid*, at pp 403, 404 (Bowen LJ).

[62] See *Re Flower and Metropolitan Board of Works* (1884) 27 ChD 592.

a particular function not to some third party but to one of themselves. Certain rules were clear. First, it was of course the duty of trustees (other than charity trustees) to act both jointly and unanimously.[63] Secondly, save in cases of necessity, trustees were obliged to ensure that trust property was held in the names of all of them.[64] They would commit a breach of trust if they allowed the property to come under the sole control of one of them.[65] Even in cases of necessity, trustees would commit a breach of trust if they permitted the property to remain in the hands of the one of them who had received it longer than the circumstances required.[66] Thirdly, all the trustees had to receive any capital monies that were payable to the trust. This task could not be delegated to one alone.[67] Fourthly, it was no breach of trust for one trustee to receive the income from the trust property on behalf of the others.[68] Several reasons were given for this. One explanation was that because trustees were co-owners of the property, "every one by law may receive either all or as much of the profits as he can come by".[69] In other cases it was justified by "moral necessity".[70] Fifthly, the law deliberately discouraged the not uncommon situation of "passive delegation". It was well-settled that "where several trustees leave the entire performance of the duties of the trust to one, all are equally responsible for the faithful and diligent discharge of their joint and several duty by that one to whom they have delegated it".[71] Finally, trustees were not entitled to remuneration for their work (except in exceptional circumstances), unless authorised by the trust instrument.[72]

3.15 Although the point was not free from doubt, and there were statements to the contrary, there was authority that one trustee could be engaged by the others to act as their agent on behalf of the trust.[73] This was subject to the restrictions set out in the previous paragraph and appears to have been limited to those matters that could be properly delegated to an agent. Certainly, if a trustee was so engaged, he was to be treated "exactly in the same way as if [the other trustees] had appointed a stranger as agent".[74]

Statutory powers to employ agents

[63] "There is no law that I am acquainted with which enables the majority of trustees to bind the minority": *Luke v South Kensington Hotel Co* (1879) 11 ChD 121, 125, *per* Jessel MR. Charity trustees may act by a majority.

[64] There were cases where a company did not permit the registration of shares in joint names, so that they had to be placed in the name of just one trustee: see, eg, *Consterdine v Consterdine* (1862) 31 Beav 330; 54 ER 1165.

[65] See, eg, *Rodbard v Cooke* (1877) 36 LT 504.

[66] See *Brice v Stokes* (1805) 11 Ves 319, 327; 32 ER 1111, 1114.

[67] *Re Bellamy and Metropolitan Board of Works* (1883) 24 ChD 387; above, para 3.13.

[68] *Townley v Sherborne* (1633) J Bridg 35; 123 ER 1181; *Williams v Nixon* (1840) 2 Beav 472, 475, 476; 48 ER 1264, 1265, 1266.

[69] *Townley v Sherborne*, above, at p 37; 123 ER at 1183; *per curiam*.

[70] This might be the case where the regulations of a company provided that where stocks and shares were registered in joint names, dividends were to be paid to the person whose name first appeared on the register.

[71] *Oliver v Court* (1820) 8 Price 127, 167; 146 ER 1152, 1167, *per* Richards LCB.

[72] See Part X of this Paper.

[73] See *Home v Pringle* (1841) 8 Cl & Fin 264, 286 - 288; 8 ER 103, 113.

[74] *Toplis v Hurrell* (1854) 19 Beav 423, 427; 52 ER 414, 416, *per* Romilly MR.

3.16 The circumstances in which trustees may delegate their functions to agents are now regulated by statute. These statutory powers "are in addition to the powers conferred by the instrument, if any, creating the trust".[75] However they apply "if and so far only as a contrary intention is not expressed" in that instrument, and have effect subject to its terms.[76] They are therefore default powers, which a settlor may add to, exclude or vary.

3.17 The statutory regime is concerned not just with the circumstances in which trustees may delegate but with their liabilities for the agents they employ. When looked at as a whole, it does not cohere very effectively. In part at least, this is because it is comprised of a patchwork of provisions that were not conceived of as an entirety but were enacted at different times - even though they now happen to be contained in the same statute. Some of the provisions are concerned with the collective delegation of functions by all the trustees, while others permit delegation by individual trustees. Our concern is primarily with the former as the latter have already been the subject of a Law Commission Report that has been accepted by the Government.[77] We also refer to the special position of charities and pension trusts. The relevant statutory provisions are to be found in Appendix A.

Collective delegation: Trustee Act 1925, sections 23(1) and (2)

3.18 The first (and principal) provision is section 23(1) of the Trustee Act 1925, which provides—

> Trustees or personal representatives may, instead of acting personally, employ and pay an agent, whether a solicitor, banker, stockbroker, or other person, to transact any business or do any act required to be transacted or done in the execution of the trust, or the administration of the testator's or intestate's estate, including the receipt and payment of money, and shall be entitled to be allowed and paid all charges and expenses so incurred, and shall not be responsible for the default of any such agent if employed in good faith.

3.19 This subsection, which was introduced as part of Lord Birkenhead's reforms,[78] appears to have been based on a common form clause then in use.[79] Its effect was considered in *Re Vickery*,[80] where Maugham J held that it abolished the limitation on trustees' powers to delegate their functions only in cases of moral necessity. He observed that—

> [i]t is hardly too much to say that it revolutionizes the position of a trustee

[75] Trustee Act 1925, s 69(2).

[76] *Ibid*.

[77] The Law of Trusts: Delegation by Individual Trustees (1994) Law Com No 220.

[78] It was first enacted as Law of Property Act 1922, s 125(1) (which was never brought into force) and then consolidated in the present subsection.

[79] In the commentary on the section in Sir Benjamin Cherry, D H Parry and J R P Maxwell, *Wolstenholme & Cherry's Conveyancing Statutes* (12th ed 1932 - the last edition to be edited by the draftsman of the section, Sir Benjamin Cherry) Vol 2, p 1299, it is stated that the subsection "renders unnecessary the common form, save that no power is given for a professional trustee to charge".

[80] [1931] 1 Ch 572, 581.

> or an executor so far as regards the employment of agents. He is no longer required to do any actual work himself, but he may employ a solicitor or other agent to do it, whether there is any real necessity for the employment or not. No doubt he should use his discretion in selecting an agent, and should employ him only to do acts within the scope of the usual business of the agent...[81]

Although other aspects of *Re Vickery* are controversial,[82] this one is generally assumed to be correct.[83] Given the explicit wording of the subsection, it is difficult to see what function section 23(1) could otherwise have.[84] However, as we explain in the following paragraphs, there are—

(1) some very significant limitations on trustees' powers of delegation; and

(2) a number of material doubts about the scope of these powers.

NO DELEGATION OF FIDUCIARY POWERS EXCEPT IN RELATION TO PROPERTY ABROAD

3.20 First, section 23(1) authorises trustees to delegate their ministerial powers but not their fiduciary discretions.[85] As the Law Reform Committee explained in its Twenty-third Report,[86] the subsection "is a power to employ agents to do specified acts and is not a power to authorise agents to decide what acts to do."[87] Although when section 23(1) was first enacted, this limitation was not regarded by commentators as being in any

[81] Cf *Green v Whitehead* [1930] 1 Ch 38, 45, where Eve J was more cautious. In remarks, which were addressed to s 23 as a whole (he was concerned primarily with s 23(2) which is considered below, para 3.20), he stated that the section "no doubt gives to the trustees enlarged and somewhat wide powers of employing agents...".

[82] See below, paras 4.39 and following.

[83] See, eg Robert D Carswell, *Trustee Acts (Northern Ireland)* (1964) p 55 (commenting on Trustee Act (Northern Ireland) 1958, s 24(1), which is similar but not quite identical to Trustee Act 1925, s 23(1)). See too Dennis Paling, "Trusteeship: The Duty to Act Personally" (1975) 125 NLJ 56.

[84] See Gareth Jones, "Delegation by Trustees: A Reappraisal" (1959) 22 MLR 381, 393.

[85] See *Green v Whitehead* (1929) 142 LT 1, 49 TLR 11 (CA). In that case two trustees for sale had contracted to sell certain land to a purchaser. They tendered a conveyance which was executed by one of them and by an attorney appointed by the other under a wide power of attorney which purported to delegate "the sole and absolute control of all my property real and personal of every description...". Eve J looked at the terms of the power of attorney and held that such a wide delegation exceeded what was permissible under s 23: [1930] 1 Ch 38. On appeal, the Court of Appeal looked at the *function* that it was sought to delegate - the execution of a conveyance - rather than the *width* of the power of delegation. As Lawrence LJ explained, "[h]ere no question arises of any exercise of the trustees' discretion by an attorney because the trustees themselves have entered into the contract for sale. The delegation of the ministerial act of executing the conveyance was... authorised by section 23 of the Trustee Act 1925...": (1929) 142 LT 1, 4 (cf 49 TLR 11, 12, where Lord Hanworth MR's judgment is rather cryptically reported). However, the Court went on to hold that that power did not authorise the disposition of property held on trust for sale and therefore affirmed Eve J. See too Robert D Carswell, *Trustee Acts (Northern Ireland)* (1964) p 55.

[86] The Powers and Duties of Trustees (1982) Cmnd 8733, para 4.3.

[87] See to like effect Pension Law Reform: The Report of the Pension Law Review Committee (Chairman: Professor Roy Goode) CM 2342-1 (September 1993), para 4.9.27. For convenience this is referred to hereafter as "the Goode Report".

sense axiomatic - quite the reverse[88] - it is in fact apparent when the subsection is contrasted with section 23(2). The latter gives trustees and personal representatives the power to delegate to an agent the execution or exercise of "any discretion or trust or power vested in them" in relation to any property which is either subject to the trust or forms part of the deceased's estate that is situated outside the United Kingdom.[89] Subsection 23(2) is of course declaratory of the effect of the decision of the Privy Council in *Stuart v Norton*,[90] and was intended to be so.[91] Section 23(2) must necessarily qualify section 23(1): the subsection would have been unnecessary if section 23(1) had been intended to enable trustees to delegate their fiduciary discretions. Ironically, by enacting these two subsections, Parliament precluded any relaxation that might otherwise have taken place at common law of the rule against the delegation of such discretions.[92]

NO SUB-DELEGATION EXCEPT IN RELATION TO AGENTS ABROAD

3.21 Secondly, although section 23(1) permits delegation of trustees' ministerial functions, it does not appear to authorise them to confer on any agent they appoint a power to subdelegate that function. Section 23(2) expressly provides that where a trustee does delegate his or her discretions, he or she may give the agent "a power to appoint substitutes". In the absence of any similar provision in section 23(1), it is again inferable that it confers no equivalent power.

[88] It was (for example) suggested that ss 23(1) and (2) would "revolutionize this particular branch of the law of trusts by dispensing with trustees from the maxim '*delegatus non potest delegare*'; it is no mere occasional employment of certain special agents for special purposes, but a general delegation of any kind of business of the trust to an agent chosen by the trustee himself, that is contemplated...": H G Hanbury, *Godefroi on the Law of Trusts* (5th ed 1927) p 197.

[89] See too Trustee Act 1925, s 25(1), as originally enacted (it has since been substantially amended by the Powers of Attorney Act 1972), which provided that trustees who were intending to remain outside the United Kingdom for more than a month could by power of attorney delegate "all or any trusts, powers, and discretions vested in him as such trustee".

[90] (1860) 14 Moo PC 17; 15 ER 212; above, para 3.10.

[91] See Sir Benjamin Cherry, D H Parry and J R P Maxwell, *Wolstenholme & Cherry's Conveyancing Statutes* (12th ed 1932) Vol 2, p 1300. The subsection was first enacted as Law of Property Act 1922, s 125(2).

[92] Cf para 3.11, above.

THE ACT DELEGATED MUST BE ONE WHICH IS "REQUIRED TO BE TRANSACTED OR DONE"

3.22 Although trustees may now "employ and pay agents" to carry out tasks which they might have undertaken themselves, the act which they delegate must however be one which is "required to be transacted or done in the execution of the trust".[93] If trustees employed an agent to transact some business that was not required, they could not look to the trust fund to be indemnified for the cost. While trustees are entitled to be reimbursed out of the trust fund for "all expenses incurred in or about the execution of the trusts or powers",[94] this right is subject to the qualification that "the costs and expenses in question must have been properly incurred".[95]

NO POWER TO EMPLOY AN AGENT ON A RETAINER?

3.23 There is a doubt as to whether section 23 permits trustees to delegate functions to an agent on a general retainer. We are aware that the wording of it has been taken by some to suggest that the authority that it confers is confined to the delegation of *specific* acts or *particular* business.[96] If that is the case (and we respectfully doubt that it is), the section would appear to have curtailed the powers of delegation that trustees had formerly enjoyed at common law. It was never suggested prior to 1926 that trustees could not (for example) delegate the management of an estate to an agent on a long term basis.[97] The difficulty with any limitation of this kind - if it exists - is that it is in practice very difficult to draw a clear line between delegation of specific acts and delegation under a general retainer.

THE TERMS ON WHICH AGENTS MAY BE EMPLOYED

3.24 Another area of doubt which is not widely explored either in the authorities or in academic writing, concerns the terms on which trustees may employ agents.[98] Although the point is of considerable practical importance,[99] the sum of judicial authority on it appears to be a late nineteenth century case in which it was held that trustees had to consider carefully the terms on which they employed agents and could not simply accept without question the conditions that they were offered.[100] Two situations are of particular significance in modern trust administration.

3.25 The first concerns the extent to which trustees may agree to an exclusion of liability on the part of any agents whom they employ. This is comparatively straightforward. Section 23(1) of the Trustee Act 1925[101] itself exempts trustees from liability for the

[93] Trustee Act 1925, s 23(1).

[94] Trustee Act 1925, s 30(2), re-enacting legislation that dates back to Lord St Leonards' Act 1859 (Law of Property and Trustees' Relief Amendment Act, 22 & 23 Vict c 35, s 31).

[95] *Holding and Management Ltd v Property Holding and Investment Trust Plc* [1989] 1 WLR 1313, 1324, *per* Nicholls LJ.

[96] Cf David J Hayton, "Trustees and the New Financial Services Regime" (1989) 10 Co Law 191.

[97] See *Home v Pringle* (1841) 8 Cl & Fin 264; 8 ER 103; *Re Muffett* (1887) 56 LJCh 600.

[98] See however, P D Finn, *Fiduciary Obligations* (1977) paras 469, 470; and Andrew Mortimer, "Trustees and Investment Management: Part II" (1994) 2 Private Client Business 160, 162.

[99] Cf para 2.21, above.

[100] *Re Weall* (1889) 42 ChD 674, 678; below, para 4.2.

[101] See above, para 3.18.

defaults of any agent "if employed in good faith". As we shall explain in Part IV of this Paper, those words appear to have been interpreted literally, so that trustees are exempt from liability in the absence of bad faith on their part.[102] If that is so, it seems reasonable to infer from the subsection that trustees can properly engage an agent on the basis that he or she will not be liable for negligence in the performance of the agency.[103]

3.26 The second situation is much more difficult. It is whether trustees have power to authorise an agent to act contrary to what would otherwise be his or her fiduciary obligations - in other words, to permit those agents to engage in conduct which the trustees themselves could not.[104] Obvious examples would be where, by contract, an agent reserved the right to—

(1) sell his or her own property to the trust;

(2) purchase property from the trust; or

(3) receive some additional commission or in some other way profit from the agency.[105]

This point is of course of some importance in practice, particularly where a discretionary fund manager is employed. As we have explained, under the IFMA Terms,[106] a discretionary fund manager is authorised to enter into transactions in which it has a material interest and which may involve a potential conflict with its duty to the customer. Indeed, it may "in exceptional circumstances, deal in securities as principal" with its customer.[107]

3.27 Regarding the matter purely as one of principle, the proper approach might perhaps be as follows. It is intrinsically undesirable that agents should be employed on terms which sanction a conflict of duty and interest. However, that consideration should be

[102] See below, paras 4.34, 4.40.

[103] It is unnecessary to consider the case of a clause in the contract of agency which purported to exclude liability by the agent for his or her fraud, because "[i]t seems unlikely that such a provision would now be regarded as effective": G H Treitel, *The Law of Contract* (9th ed 1995) p 223. It has recently been decided by the Court of Appeal that a clause in a trust instrument which excluded the liability of trustees for gross negligence was not contrary to public policy: see *Armitage v Nurse*, *The Times*, 31 March 1997. In that case, Millett LJ accepted that "there is an irreducible core of obligations owed by the trustees to the beneficiaries and enforceable by them which is fundamental to the concept of the trust. If the beneficiaries have no rights enforceable against the trustees there are no trusts". However, the core obligations that were central to the existence of a trust did not include "the duties of skill and care, prudence and diligence".

[104] See above, para 2.23. As we have explained, there is no longer any doubt that fiduciaries may modify or exclude the scope of their fiduciary duties: see *Kelly v Cooper* [1993] AC 205; above, para 2.20.

[105] Cf IFMA Terms, cl 14; above, para 2.21. There must of course be limits to what an agent could do if authorised to profit from the agency. If he or she received a bribe in fraud of the principal, such a clause would not protect him or her from liability.

[106] Cls 14, 15; see above, paras 2.21(5) and (6); 2.23.

[107] IFMA Terms, cl 14(c)(vii).

weighed against any safeguards that may exist,[108] the necessity for the particular task to be undertaken, and the lack of any effective alternative.[109] In other words, although section 23(1) of the Trustee Act 1925 confers a wide power to delegate ministerial tasks, that power ought not to be exercised if, on balance, the risks were too high so that the trustees would be failing in their paramount obligation to act in the best interests of the beneficiaries.[110] It might (for example) be reasonable for trustees to authorise specific acts of self-dealing but not to give a general authority to self-deal. All of this presupposes that trustees have power under section 23 to authorise such acts, but this may not be the case. It may be that trustees cannot authorise others to do what they themselves have no power to do.

3.28 There does in fact appear to be no direct authority on whether trustees who engage agents on terms which sanction a conflict of interest thereby commit a breach of trust,[111] and if they do, what the basis of that breach might be.[112] Instead, the issue has tended to arise only obliquely in proceedings against an agent employed by the trustees, alleging breach of his or her fiduciary obligations. The agent claims to be absolved from liability because he or she acted with the fully informed consent of the trustees. Even if the agent is absolved, it does not necessarily follow that the trustees had the power to agree to such terms. The trustees might have been acting in breach of trust, but one to which the agent was not privy.

3.29 An issue that is raised in a number of cases is whether, where an agent is employed by trustees, he or she may owe fiduciary obligations not merely to the trustees as principal but also to the beneficiaries under the trust. It is clear that no such fiduciary obligations arise merely from the fact of employment by the trustees.[113] While there are undoubtedly situations in which an agent will owe such duties,[114] what these circumstances may be has never been stated definitively. Although there is some

[108] See, eg in relation to the employment of discretionary managers, the obligation on the manager in cases of conflict that the transactions are not effected on terms any less favourable than would be the case if there were no potential conflict: IFMA Terms, cl 14(b).

[109] Such alternatives might include (i) the availability of other agents of similar competence who would not insist upon such terms, even if, they might perhaps be more expensive to employ; or (ii) other possible methods of achieving the objective desired by the trustees. We doubt that trustees will very often find themselves in a position where they have no effective option but to agree to such terms.

[110] See above, para 2.1.

[111] It is clear that a fiduciary may seek the authority of the court to employ an agent where there may be a conflict between the agent's duties to the fiduciary and those owed by him or her to another principal. Thus in *Re Schuppan (a bankrupt)* [1996] 2 All ER 664, the court gave authority for a trustee in bankruptcy to retain the petitioner's solicitors to act for him as well. The facts were very carefully scrutinised.

[112] There are at least three possible reasons why there *might* be a breach of trust in such circumstances. First, the trustees might have no power at all to employ agents on such terms. Secondly, they might not have exercised the appropriate standard of care in agreeing the terms of appointment of such agents (see Part IV of this Paper). Thirdly, in employing agents on such terms they might have been acting in breach of their paramount obligation to exercise their powers in the best interests of the beneficiaries.

[113] *Bath v Standard Land Co Ltd* [1911] 1 Ch 618; below, para 3.31. But cf *Boardman v Phipps* [1967] 2 AC 46, 112, where Lord Hodson considered that the defendant was "in a fiduciary position *vis-à-vis* the trustees and through them *vis-à-vis* the beneficiaries".

[114] See F M B Reynolds, *Bowstead and Reynolds on Agency* (16th ed 1996) Article 37(3), paras 5-008, 5-011; approved in *Henderson v Merrett Syndicates Ltd* [1995] 2 AC 145, 202.

authority which suggests that there will be such a duty if the agent knows (from whatever source) of the fact that he or she is acting on behalf of a trust,[115] in other cases the courts have declined to find a fiduciary relationship from such knowledge alone.[116] The nature of the agent's conduct, or the task which he or she has undertaken, may have a bearing on the issue. Thus the courts have found such a direct fiduciary relationship where an agent has received a bribe from a third party,[117] and where an agent employed to sell trust property purchased it for himself.[118] A number of the cases on whether an agent owes fiduciary duties to someone other than his or her immediate principal, have not involved trustees at all. They have been situations where A has employed an agent B, who in turn has sub-delegated to C.[119] The issue has been whether C owes fiduciary duties directly to A. These cases are not precisely analogous to the situation where B, who holds on trust for A, employs an agent, C. Unless they are nominees, trustees do not act at the direction of the beneficiaries, but independently, in accordance with their obligations under the trust. The justification for a fiduciary relationship between C and A is commensurately much weaker.

3.30 Where the agent *does* stand in a fiduciary position to the trust, his or her fiduciary obligations are the same as those of the trustees themselves.[120] Furthermore, there is some authority that suggests that only the beneficiaries can authorise that agent to act in a manner that would be in breach of those fiduciary duties.[121] If these decisions are correct—

(1) there will necessarily be some cases where such consent is either legally or factually unobtainable, as for example in the case of a trust with infant or unborn beneficiaries or a discretionary trust with a large class of objects; and

[115] See *Powell & Thomas v Evan Jones & Co* [1905] 1 KB 11 and the dissenting judgment of Fletcher Moulton LJ in *Bath v Standard Land Co Ltd* [1911] 1 Ch 618, 631 - 641.

[116] See *New Zealand and Australia Land Co v Watson* (1881) 7 QBD 374; the actual decision in *Bath v Standard Land Co Ltd*, above; and *Royal Products Ltd v Midland Bank Ltd* [1981] 2 Lloyd's Rep 194, 198.

[117] *Powell & Thomas v Evan Jones & Co*, above. It should be noted that persons who receive bribes are not infrequently characterised as "fiduciaries" in circumstances where they would not be for any other purpose. Thus persons holding public office, such as a sergeant in the police or the army, or a public prosecutor (see respectively, *Attorney-General v Goddard* (1929) 98 LJKB 743; *Reading v Attorney-General* [1951] AC 507; and *Attorney-General for Hong Kong v Reid* [1994] 1 AC 324) would not normally be treated as a fiduciary in the same way as a trustee or a company director would be.

[118] One of the justifications for the "self-dealing" rule, which prohibits a trustee from purchasing trust property is that the trustee "is bound by his duty to acquire all the knowledge possible, to enable him to sell to the utmost advantage for the *cestui que trust*": *Ex p James* (1803) 8 Ves 337, 348; 32 ER 385, 389, *per* Lord Eldon LC (a case involving a sale by a trustee in bankruptcy). The mere risk that the trustee *may* have acquired knowledge that others could not have done, debars him or her from purchasing the property: see *Ex p Lacey* (1802) 6 Ves 625; 31 ER 1228. Any agent whom the trustee employs to sell is, for the same reason, considered to be subject to the same disability: *Ex p Bennett* (1805) 10 Ves 381, 396; 32 ER 893, 898; *Re Bloye's Trust* (1849) 1 Mac & G 488, 496; 41 ER 1354, 1357.

[119] See, eg *Powell & Thomas v Evan Jones & Co*, above.

[120] See, eg *Ex p James* (1803) 8 Ves 337, 345 - 7; 32 ER 385, 388; *Ex p Bennett* (1805) 10 Ves 381, 396; 32 ER 893, 898; *Whitcomb v Minchin* (1820) 5 Madd 91; 56 ER 830; *Re Bloye's Trust* (1849) 1 Mac & G 488, 496; 41 ER 1354, 1357; *Martinson v Clowes* (1882) 21 ChD 857, 860.

[121] See, eg *Ex p James*, above at p 352; 32 ER at p 391; *Re Bloye's Trust*, above at p 494; 41 ER at 1356; *Bath v Standard Land Co Ltd* [1911] 1 Ch 618, 637.

(2) trustees can never authorise their agents to act in what would otherwise be contrary to their fiduciary obligations.

3.31 However, there are other decisions which may support the view that the trustees can sanction at least some types of breach of fiduciary duty by the agent, though it is not always clear from these cases whether the agent was regarded as standing in a fiduciary relationship to the beneficiaries under the trust. The first case is *Bath v Standard Land Co Ltd*,[122] in which the plaintiff, who was bankrupt, believing that his lands in Kent were worth more than his liabilities, transferred them to the defendant company as trustee to "manage, develop, realise or dispose of". To do this, the company employed a number of its officers and employees to realise the assets,[123] allowing them to charge not only for their expenses but a profit element as well. The issue arose as to whether the company could charge the plaintiff for that profit. The Court of Appeal, by a majority, held that it could.[124] The company could plainly have employed and paid agents to carry out the various tasks for which the officers and employees had been employed, and that payment could have included a profit element. The fact that those agents were officers or employees of the company did not mean that they stood in a fiduciary relationship to the plaintiff beneficiary, nor did it preclude them from being paid the same profit element that could have been paid to any agent who was not connected to the company.[125] The second case - *Regal Hastings Ltd v Gulliver*[126] - did not involve a trust at all but a company. A solicitor acting for company A, was asked by its directors to take shares in company B. He did so and profited substantially from it, as did the directors themselves. The House of Lords held that, although by virtue of their fiduciary position, the directors were accountable to company A for the profits that they had made from the transaction,[127] the solicitor was not. He purchased the shares at the express request of the company - acting through its directors rather in general meeting. A third and somewhat similar case is *Nutt v Easton*,[128] where the executrix of a mortgagee of a reversionary interest, exercising her power of sale as mortgagee, requested the solicitor who had obtained probate of the deceased's will, to purchase the reversion. The solicitor, who had attempted, without success, to find a purchaser for the interest, reluctantly acceded to the executrix's request. He paid more than the actuarial value for it. He also informed the mortgagor of the sale. The mortgagor took legal advice, was told that he could have the sale set aside, but despite this, did nothing. When he attempted to do so ten years later, his claim was dismissed. Although the claim was barred by laches, Cozens-Hardy J also doubted that the executrix could have had the sale set aside in the circumstances.

[122] [1911] 1 Ch 618.

[123] These were a solicitor who was a director; an accountant, who was company secretary; an estate agent who was employed by the company to manage certain properties; and an auctioneer who was habitually used by the company in its business.

[124] See particularly the judgment of Buckley LJ at [1911] 1 Ch 618, 642 - 647.

[125] The articles of the company did in fact expressly permit directors to profit from any contract which they made with the company.

[126] [1942] 1 All ER 378; [1967] 2 AC 134n.

[127] The directors could not authorise their own conflict of duty and interest, but only the company in general meeting.

[128] [1899] 1 Ch 873.

3.32 A particularly difficult case in this regard is *Boardman v Phipps*.[129] The salient facts were that A and B, profited from what a majority of the House of Lords held to be their fiduciary relationship to the Phipps trust. The plaintiff, a beneficiary under the trust, successfully sought to make A and B account to the trust for that profit. In what they did, A and B had acted with the knowledge of two of the three trustees. The third trustee was suffering from senile dementia and "was not really fit to be a trustee".[130] Although they had made partial disclosure to the plaintiff, they failed to tell him all of the material facts.[131] The issue whether, if there had been three trustees who were capable of acting, they could have authorised A and B to make their profit, did not of course arise given the facts. In the particular circumstances it was impossible to obtain the consent of the trustees,[132] and A and B could have escaped liability *only* if they had obtained the fully informed consent of the beneficiaries.[133] This may explain why a number of judges expressed the view that A and B could not profit from their position *without the consent of the beneficiaries*.[134] However, it is significant that, in the passage of the case, a number of judges considered that the consent of—

(1) all the trustees;[135] or

(2) either all the trustees or the beneficiaries;[136]

would have sufficed to exculpate A and B.

3.33 In the light of the authorities, whether trustees can sanction agents to enter into transactions that they themselves could not, cannot be regarded as finally resolved. There must be a doubt whether, in the absence of some express or implied authority in the trust instrument, trustees have any *power* to enter into such a contract. Even if they do, it may be a breach of trust for them to give such authority, at least in relation to certain types of conduct.

Collective delegation: Trustee Act 1925, section 23(3)

3.34 Section 23(3) of the Trustee Act 1925 re-enacts, with amendments, provisions derived from earlier legislation.[137] These had been introduced not to lay down any broad principles defining the circumstances in which trustees could delegate but to deal with specific practical problems, some of which had been thrown up by judicial decisions. Thus the effect of section 23(3)(*a*) is that trustees, when selling land, can, like any

[129] [1967] 2 AC 46.

[130] See the case in the Court of Appeal (*sub nom Phipps v Boardman*): [1965] Ch 992, 1011, *per* Lord Denning MR.

[131] At first instance, Wilberforce J held that the plaintiff "was fully justified in thinking that he had only been told half the truth": [1964] 1 WLR 993, 1017.

[132] Because one was not in a state of health in which she could consent.

[133] See Wilberforce J: [1964] 1 WLR 993, 1012 (at first instance); and Viscount Dilhorne: [1967] 2 AC 46, 93 (HL).

[134] See Lords Cohen and Hodson in the House of Lords: [1967] 2 AC 46 at 104 and 112 respectively.

[135] See by inference, Russell LJ: [1965] Ch 992, 1031, 1032 (CA), and explicitly, Lord Guest: [1967] 2 AC 46, 117 (HL).

[136] See Pearson LJ: [1965] Ch 992, 1023 (CA); Viscount Dilhorne: [1967] 2 AC 46, 93 (HL).

[137] See Trustee Act 1893, s 17.

other vendor, authorise their solicitor to receive the purchase money and give a good discharge for it, provided that the trustees have signed a receipt, either in the body of or endorsed on the deed of conveyance or transfer.[138] The inconvenient position at common law, which this provision reversed, was that the receipt of capital monies was a fiduciary function that trustees could not delegate. As a result they had to receive the purchase price personally.[139] Section 23(3)(*c*), which is of a similar character to section 23(3)(*a*), enables trustees to delegate to a banker or solicitor the power to receive and give a valid discharge for any money payable under an insurance policy. It should be noted that these specific powers to delegate are given "without prejudice to such general power of appointing agents" conferred by section 23(1).

Delegation by individual trustees: Trustee Act 1925, section 25

3.35 Section 25 of the Trustee Act 1925 provides a means by which an individual trustee can temporarily delegate those "trusts, powers and discretions vested in him as trustee". When first enacted, it was confined to "a trustee intending to remain out of the United Kingdom for a period exceeding one month".[140] However, the circumstances in which trustees may delegate their trusts for short periods have been widened in recognition that a trustee's inability to attend to trust affairs may arise for reasons other than absence abroad. The section in its present form derives from section 9 of the Powers of Attorney Act 1971. That Act gave effect to recommendations made in a Law Commission Report.[141] The operation of the amended section 25 was further reviewed by the Commission in a subsequent Report, The Law of Trusts: Delegation by Individual Trustees.[142] In that latter Report,[143] we described the effect of section 25 as follows—

> Section 25, as amended, provides that a trustee[144] may, by power of attorney, delegate the exercise of his powers and duties for a period not exceeding twelve months,[145] but not to his sole co-trustee (unless a trust corporation).[146] He must give notice of the creation of the power and the reason for the delegation to each person entitled to appoint new trustees and to his co-trustees.[147] The donor remains liable for the acts and defaults of the attorney.[148] Special protection [149] is given in some stock transactions;

[138] Cf Law of Property Act 1925, s 69.

[139] See *Re Bellamy and Metropolitan Board of Works* (1883) 24 ChD 387; *Re Flower and Metropolitan Board of Works* (1884) 27 ChD 592; above, para 3.12.

[140] The provision in the 1925 Act was based on similar temporary provisions in the Trusts (War Facilities) Acts 1914 and 1915 - a clear indication of the original purpose of the section.

[141] Powers of Attorney (1970) Law Com No 30.

[142] (1994) Law Com No 220.

[143] At para 2.5. Certain details from the footnotes have been omitted: these are indicated thus— "...".

[144] "Trustee" includes a personal representative: Trustee Act 1925, s 25(8).

[145] *Ibid*, s 25(1).

[146] *Ibid*, s 25(2)...

[147] *Ibid*, s 25(4).

[148] *Ibid*, s 25(5).

[149] In addition to the general protection afforded to those dealing with attorneys against the revocation of the powers without their knowledge: Powers of Attorney Act 1971, s 5.

those in whose books the stock is inscribed or registered are not affected by notice of any trust even though its existence is apparent on the face of the power.[150]

3.36 What section 25(1) of the Trustee Act 1925 permits - that section 23 does not - is the delegation of "the execution or exercise of all or any of the trusts, powers and discretions". However, unlike the powers conferred by section 23, it is conferred on trustees *individually* and not collectively. It is of course the case that if all the trustees are so minded, they may each choose to delegate all or some of their powers to the same particular delegate under this section. In this way, trustees can, in effect, delegate their fiduciary powers (such as powers of investment) to an agent. There are however a number of significant impediments to this device as a means by which trustees may routinely delegate their fiduciary powers.[151]

3.37 Those impediments may be summarised as follows—

(1) any such delegation is limited to a period of twelve months;[152]

(2) doubts have been expressed as to whether it is an appropriate exercise of the power to renew the delegation annually;[153]

(3) even if such a renewal is proper, if it is not made by the trustees due to some oversight, or if the exercise of the power is delayed, the trustees will be in breach of trust if the delegate continues to exercise the power;

(4) a trustee who makes such a delegation, is required to give notice of it within seven days to each of the other trustees and to every person who, under the trust instrument, has a power to appoint new trustees;[154]

(5) each of the trustees is vicariously liable for the acts or defaults of his or her

[150] Trustee Act 1925, s 25(7)...

[151] The Law Commission reviewed the working of Trustee Act 1925, s 25 in its report, The Law of Trusts: Delegation by Individual Trustees (1994) Law Com No 220, paras 4.5 - 4.17, and while suggesting certain changes in the scope of s 25, recommended that there should be no material change to the requirements that are in issue here. The one change recommended by the Commission that is noteworthy is the abolition of the prohibition against delegating to a sole co-trustee in s 25(2): see Delegation by Individual Trustees, above, paras 4.11 and following.

[152] Trustee Act 1925, s 25(1). In The Law of Trusts: Delegation by Individual Trustees (1994) Law Com No 220, at para 4.6 we commented that "[t]his time limit is arbitrary, but we found no great pressure [ie, on consultation] to change it. The assessment of the appropriate length of delegation is essentially a matter of balancing the practical convenience of those who use these powers of attorney against the possibilities of abuse. The evidence we received suggested that the present balance was satisfactory. *We recommend* no change".

[153] It has been suggested that the permanent use of the power in this way "is [not] reasonably within the contemplation of the statute": Leolin Price, QC, "Further trust problems" (1993) 137 SJ 535. Even if annual renewal is not intrinsically improper, it is plainly not the purpose of the section to enable long-term or permanent delegation. Indeed, in the Report that led to the enactment of the Powers of Attorney Act 1971, Powers of Attorney (1970) Law Com No 30, para 22, we made it clear that the need to renew the power every year acted as a deterrent to permanent delegation, and would "deter excessive use of this facility".

[154] Trustee Act 1925, s 25(4).

delegate,[155] whereas trustees who delegate under section 23(1) are not;[156]

(6) unlike section 23(1), there is apparently no power when delegating under section 25(1) to remunerate the delegate;[157] and

(7) the delegate cannot sub-delegate the powers reposed in him or her.[158]

3.38 Although these features of any delegation under section 25 of the Trustee Act 1925 can be regarded as "impediments" to the use of that section as a means by which trustees might collectively delegate their fiduciary obligations, it should be emphasised that the section was never intended to perform that rôle, nor do we think it desirable that it should. In recommending the reformulation of section 25 into its present form,[159] we considered that what was needed was—

> some reasonably simple and flexible machinery enabling the trustee to delegate his powers for moderate periods when this is necessary but which does not make delegation so easy as to encourage trustees to neglect their personal responsibilities without sufficient cause.[160]

We adhered to that view of the section in our Report, The Law of Trusts: Delegation by Individual Trustees,[161] where we emphasised that the "impediments" listed in paragraph 3.37 above, operated in fact as "safeguards for beneficiaries".[162] In short, the object of section 25 - both in its original and in its present recast form - has always been to enable an *individual* trustee to delegate his or her trusts in circumstances where, for some comparatively short period, it was likely to be difficult or impossible to perform them, but where he or she intended to resume them thereafter.[163] It is not therefore surprising that it makes no provision (for example) for the payment of any delegate.[164]

[155] *Ibid*, s 25(5). Because of this vicarious liability, it may be that the delegate is to be regarded as the substitute for the trustee. If that is so, the delegate can do nothing that the trustee could not do. A trustee could not therefore authorise a delegate to engage in transactions where there was a conflict of duty and interest. Cf IFMA Terms, cl 14(a); above, para 2.21(5).

[156] See below, para 4.30.

[157] Goode Report, para 4.9.28; Law Reform Committee, 23rd Report, The Powers and Duties of Trustees (1982) Cmnd 8733, para 4.19.

[158] Trustee Act 1925, s 25(6). This point can in practice be significant: see above, para 2.23.

[159] Prior to the enactment of the Powers of Attorney Act 1971, s 9 (which substituted the present s 25), an individual trustee could delegate his or her powers under Trustee Act 1925, s 25 only where he or she intended to remain out of the United Kingdom for more than one month.

[160] Powers of Attorney (1970) Law Com No 30, para 17.

[161] (1994) Law Com No 220, para 3.1, where we said: "There will inevitably be times when the trustee cannot personally attend to the affairs of the trust, perhaps because of illness or absence, and it is useful to be able to ensure that the trust is not neglected. If it were not possible to appoint a temporary substitute, the only course might be for the trustee to resign and be replaced."

[162] *Ibid*, para 3.4. See too para 3.6.

[163] We referred to the common thread that linked the different forms of section 25 as being "the equitable principle that complete delegation of trustee functions should be possible only in specific circumstances": *ibid*, para 2.4.

[164] Trustees are normally expected to act without payment unless the trust instrument sanctions it. See below, Part X.

Delegation by individual trustees: Enduring Powers of Attorney Act 1985, section 3(3)

3.39 Any delegation under section 25(1) of the Trustee Act 1925 has to be made by means of a power of attorney. A power of attorney is automatically revoked by the mental incapacity of the donor.[165] It became possible, as a result of the Enduring Powers of Attorney Act 1985,[166] to execute an enduring power of attorney that was not automatically revoked in such circumstances. Section 3 of that Act is concerned with the scope of an enduring power. Section 3(3), which was introduced during the Bill's passage through Parliament to deal with difficulties occasioned by a particular judicial decision,[167] provides that—

> Subject to any conditions or restrictions contained in the instrument,[168] an attorney under an enduring power, whether general or limited, may (without obtaining any consent) execute or exercise all or any of the trusts, powers or discretions vested in the donor as trustee and may (without the concurrence of any other person) give a valid receipt for capital or other money paid.

3.40 In our Report, The Law of Trusts: Delegation by Individual Trustees,[169] we explained that section 3(3) offered a second route by which an individual trustee might delegate his or her trusts in addition to the way provided by section 25 of the Trustee Act 1925. However, the safeguards which were applicable to a power executed under section 25 had no equivalent in relation to section 3(3) of the Enduring Powers of Attorney Act 1985. As a result of this and other criticisms,[170] we recommended that section 3(3) should be repealed,[171] and that the mischief that it was intended to remedy should be dealt with by other means.[172] As these recommendations have been accepted and will be enacted when a suitable legislative opportunity occurs,[173] it is unnecessary to consider this section further.

Charitable trusts

3.41 The rules as to when trustees may delegate apply to trustees of charitable trusts as

[165] See *Yonge v Toynbee* [1910] 1 KB 215, 228.

[166] Which implemented our Report, The Incapacitated Principal (1983) Law Com No 122.

[167] *Walia v Michael Naughton Ltd* [1985] 1 WLR 1115. The issue was whether, where three trustees for sale held land on trust for themselves as beneficial co-owners, one of them could employ the short general power of attorney conferred by Powers of Attorney Act 1971, s 10 to authorise one of the others to act in the disposition of the property. Section 10 does not apply "to functions which the donor has as a trustee": *ibid*, s 10(2). It was held that, although the trustees were beneficial co-owners, in transferring the legal title, they were exercising their functions as trustees. Their status as beneficial co-owners was therefore irrelevant. See further The Law of Trusts: Delegation by Individual Trustees (1994) Law Com No 220, paras 2.10 - 2.19.

[168] Which means the instrument creating the enduring power of attorney.

[169] (1994) Law Com No 220, para 3.11.

[170] See *ibid*, paras 3.3 - 3.13.

[171] *Ibid*, paras 3.14, 4.1 - 4.3.

[172] We recommended that a donee of a power of attorney should not be prevented from acting in relation to land in which he had a beneficial interest, thereby reversing *Walia v Michael Naughton Ltd* [1985] 1 WLR 1115: (1994) Law Com No 220, para 4.31.

[173] Written Answer, *Hansard* (HL) 22 March 1995, vol 562, col 73.

much as they do to other trustees. However, the Charity Commissioners have a statutory power to authorise dealings with charity property that would not otherwise be within the powers of the trustees.[174] This power can be and is used to authorise an extension of trustees' powers of delegation.[175] In particular, the Commissioners are willing to make an order under their statutory powers in cases where both the value of the charity's investment (which will usually have to have a value in excess of £100,000 before such an order will be considered) and the frequency of transactions is high enough to warrant their delegation to a discretionary fund manager.[176] The Commissioners have devised a Model Order for this purpose which contains specific requirements and safeguards.[177] The terms of that Model Order, which we set out in Appendix A, are considered in more detail later in this Paper.[178] They provide for reviews of the appointment of the investment manager on a biennial basis. An application of this kind to the Charity Commissioners for additional powers will involve some expense on the part of the charity.[179]

Pension trusts

PENSIONS ACT 1995, SECTION 34

3.42 We have already explained that our recommendations in relation to pensions trusts are necessarily conditioned by the provisions of the Pensions Act 1995 which relate to the delegation of investment decisions.[180] However, those provisions are in themselves very important to any proposals for reform because of the indication that they provide of Parliament's attitude to delegation by one particularly significant category of trustees.[181] First, section 34(2) of the Pensions Act 1995 provides that "any discretion of the trustees of a trust scheme[182] to make any decision about investments" may be delegated to a fund manager who satisfies certain requirements.[183] That discretion

[174] Charities Act 1993, s 26 (re-enacting provisions of the Charities Act 1960).

[175] (1994) 2 *Decisions of the Charity Commissioners*, p 29.

[176] *Ibid*.

[177] *Ibid* at p 31.

[178] See below, para 4.50.

[179] It has been estimated that an application for *an extension of investment powers* is likely to cost the charity in the region of £600 to £1,000. (The figure of £600 was given by the Charity Commissioners in its response to Investment Powers of Trustees: A Consultation Document by HM Treasury. As regards the figure of £1,000, see the Deregulation (Trustee Investments) Order 1997, Explanatory Memorandum by HM Treasury, para 28, which was based upon information supplied by one branch of the Society of Trust and Estate Practitioners.) However, we understand from the Charity Commissioners that an application for *wider delegation powers* is likely to cost substantially less than this.

[180] See above, para 1.14.

[181] The provisions derive from recommendations in the Goode Report, Chapter 4.9.

[182] Which means an occupational pension scheme established under a trust: Pensions Act 1995, s 124(1).

[183] Those requirements are that, for the purposes of the Financial Services Act 1986, the fund manager should be an authorised person (such as a member of a self-regulatory organisation, a person recognised by a professional body, etc, within Financial Services Act 1986, Part 1, Chapter III); an exempted person acting in the course of business in which it is exempt (such as an investment exchange, a clearing house, etc, within Financial Services Act 1986, Part 1, Chapter IV); or a person who does not require authorisation to manage assets (see Financial Services Act 1986, Sched 1, Part IV). See Pensions Act 1995, s 34(3); Financial Services Act 1986, s 191(2).

cannot be delegated in any other way except by an individual trustee under section 25 of the Trustee Act 1925.[184] The trustees are required to ensure that a written statement of the principles governing investment decisions for the purposes of the pension scheme is prepared, maintained and periodically revised.[185] Certain specified matters must be covered by that statement.[186] Secondly, by section 34(5) of the Pensions Act 1995, subject to any restriction imposed by the trust scheme, the trustees are empowered to delegate the exercise of their discretion to make any decisions about investments—

(1) to two or more of their number; or

(2) to a fund manager operating outside the United Kingdom as regards overseas investment business.[187]

THE GOODE REPORT AND THE RATIONALE OF SECTION 34

3.43 The background to these provisions[188] is found in the Report of the Pension Law Review Committee.[189] The Committee considered it inappropriate that pension trustees should be subject to the restrictive investment regime of the Trustee Investments Act 1961. Pension Trustees have therefore been given "the same power to make an investment of any kind as if they were absolutely entitled to the assets of the scheme".[190] As result of the provisions of the Financial Services Act 1986,[191] the trustees of a pension scheme are in practice obliged to delegate the exercise of their investment powers to a fund manager. The existing powers of delegation did not allow this. Section 23(1) of the Trustee Act 1925 enabled trustees to "engage an agent to carry out their decisions but not... to take decisions".[192] Delegation by power of attorney under section 25 of the Trustee Act 1925 was cumbersome and, in any event, might not permit the remuneration of fund managers.[193]

[184] Pensions Act 1995, s 34(2)(b). For Trustee Act 1925, s 25, see above, para 3.35.

[185] Pensions Act 1995, s 35(1). For the principles to be applied when making investments, see *ibid*, s 36.

[186] See *ibid*, ss 35(3), (4). The trustees should, for example, have a written policy on the kinds of investment to be held, the balance between different kinds of investments, risk, the expected return on investments and the realisation of investments.

[187] This states the practical effect of the form of words used in s 34(5)(b). In choosing investments, the fund manager must have regard to the principles in s 36.

[188] Subject to certain exceptions, the provisions of section 34 override any inconsistent rule of law or statutory provision: see *ibid*, s 34(7).

[189] Goode Report, para 4.9.29.

[190] Pensions Act 1995, s 34(1).

[191] Section 191; Schedule 1, para 14.

[192] Goode Report, para 4.9.27. See above, para 3.20.

[193] Goode Report, para 4.9.28. See above, para 3.37.

PART IV
TRUSTEES' POWERS OF DELEGATION: THE STANDARD OF CARE REQUIRED IN THE SELECTION AND EMPLOYMENT OF AGENTS

INTRODUCTION

4.1 In Part III, we explained what powers trustees had to delegate their functions to agents. In this Part, we consider the standard of care that is expected of trustees both when choosing such an agent under those powers and when subsequently supervising him or her. Once again we examine first the position at common law which was clear and largely uncontroversial. A full account of it is necessary to an understanding of the controversy that exists as to the present law. We then consider the law as it now is in the light of the provisions of the Trustee Act 1925 (as interpreted) and other legislation. As we explain,[1] the present law is widely regarded as unclear and unsatisfactory.

THE POSITION AT COMMON LAW

The selection of agents

4.2 Prior to 1926 the law was perfectly clear. In selecting an agent, trustees were required to exercise reasonable prudence both in choosing an agent and in negotiating the terms on which that person was employed.[2] This was no more than an application of the general principle, affirmed by the House of Lords in *Speight v Gaunt*,[3] that—

> trustees acting according to the ordinary course of business, and employing agents as a prudent man of business would do on his own behalf, are not liable for the default of an agent so employed.[4]

To escape liability for the defaults of their agents, trustees had to select persons who were "properly qualified" to carry out the task in question.[5] The matter had therefore

[1] See below, paras 4.20 and following.

[2] "A trustee is bound to exercise discretion in the choice of his agents, but so long as he selects persons properly qualified he cannot be made responsible for their intelligence or their honesty. He does not in any sense guarantee the performance of their duties. It does not, however, follow that he can intrust his agents with any duties which they are willing to undertake, or pay them or agree to pay them any remuneration which they see fit to demand. The trustee must consider these matters for himself...": *Re Weall* (1889) 42 ChD 674, 678, *per* Kekewich J. In that case, trustees were held liable for charges improperly made by an agent for work that he had never been asked to do. For a particularly clear summary of what was expected of trustees at common law when delegating, see the judgment of Chatterton V-C in *Rochfort v Seaton* [1896] 1 IR 18, 25.

[3] (1883) 9 App Cas 1.

[4] *Fry v Tapson* (1884) 28 ChD 268, 280 *per* Kay J, who also pointed out that "*Speight v Gaunt* did not lay down any new rule, but only illustrated a very old one": *ibid*. For an earlier appearance of "the ordinary prudence which a man uses in his own affairs", see *Mendes v Guedalla* (1862) 2 J & H 259, 277; 70 ER 1054, 1061, *per* Page Wood V-C.

[5] *Re Weall* (1889) 42 ChD 674, 678, *per* Kekewich J.

to be one which was within the agent's competence[6] and it was of course improper to appoint an agent who was subject to a conflict of interest.[7] Trustees were not absolved from liability however merely because they acted in good faith,[8] even though they had also acted to the limits of their own personal competence.[9]

Directions to employ an agent

4.3 A question that arose from time to time was whether trustees were *obliged* to employ an agent where a settlor, testator or beneficiary had directed them to do so. In some cases, such directions in a will were found to create a trust for the benefit of the nominated agent.[10] However, these decisions did not commend themselves to the House of Lords,[11] and the better view was that such instructions were to be regarded as expressions of wishes and were not binding on the trustees.[12] Trustees were entitled to choose the agents whom they wished to employ.[13] If trustees *did* make an appointment in accordance with the wishes of the settlor or testator, it appears that they would be under no liability as regards the *choice* of agent, even if, as prudent persons they might not have chosen that individual themselves. However, they were not relieved of their duty to exercise reasonable care in *supervising* the agent once appointed.[14]

6 See above, para 3.6.

7 *Fry v Tapson* (1884) 28 ChD 268, 282 (trustees employed mortgagor's agent to value property in which they intended to invest trust money).

8 See *Matthew v Brise* (1843) 6 Beav 239, 243; 49 ER 817, 819 (affirmed, *sub nom Mathew v Brise* (1845) 15 LJCh 39).

9 See *Re Mackay* [1911] 1 Ch 300, 307, where Parker J observed that "so far as I know no trustee has ever been held not liable for breach of trust by reason of his natural deficiencies or his lack of educational advantages. He may have acted perfectly honestly and to the best of his ability, but if he has not come up to the Court's standard of prudence, he is still held liable". That was a case where a trustee delegated a matter to an agent that was not within that agent's competence. Under a mistaken understanding of the powers conferred on him by a will, the trustee made payments to a solicitor to meet death duties. These were misappropriated by the solicitor. The trustee sought (and was granted) relief from his breach of trust under what is now Trustee Act 1925, s 61.

10 See, eg, *Williams v Corbett* (1837) 8 Sim 349; 59 ER 138.

11 See *Shaw v Lawless* (1838) 5 Cl & Fin 129, 154 - 156; 7 ER 353, 362.

12 *Finden v Stephens* (1846) 2 Ph 142; 41 ER 896; *Foster v Elsley* (1881) 19 ChD 518.

13 *Re Duke of Cleveland's Settled Estates* [1902] 2 Ch 350, 351. It does not appear to have been settled whether, if a trustee did carry out the directions of the settlor and appointed an agent who proved to be unsuitable, he could ever be liable for that agent's defaults. It is one thing to say that the trustees are absolved where the agent proposed by the settlor was one who could reasonably be employed. It is another to suggest that they could escape liability where the appointment was plainly imprudent.

14 "[I]f a testator points out an agent to be employed by the executor, I think if such an employee received a sum of money, and immediately made default, the executor would clear himself by showing that testator designated the person, and that he could not, by the exercise of reasonable diligence, recover that money. But the exercise of reasonable diligence is still required": *Kilbee v Sneyd* (1828) 2 Moll 186, 200, *per* Hart LC (Ir).

The standard of supervision

4.4 Even if trustees exercised reasonable prudence in selecting an agent, that did not excuse them from supervising that agent once appointed. In carrying out such supervision, they were once again expected to exercise "that ordinary prudence which a man uses in his own affairs".[15] It was therefore the duty of trustees to ensure that the agent was carrying out the obligations that had been delegated to him or her,[16] requiring where necessary the production of independent evidence.[17] The authorities suggest that the usual failings of trustees were in leaving trust property properly in the hands of an agent longer than was necessary,[18] and in not ensuring that instructions to invest money had been carried out.[19]

The meaning of "prudence"

4.5 As we have explained, in appointing and supervising agents, trustees were expected to exercise reasonable prudence. In *Munch v Cockerell*,[20] Lord Cottenham LC commented that—

> in charging trustees with loss from the misconduct of agents, it is not sufficient to prove that it might have been prevented by extraordinary care and caution. The trustee is not held liable if, acting strictly within the line of his duty, he exercised reasonable care and diligence.

This standard was variously formulated by reference to a number of comparisons.[21] In essence however, the question in each case was whether the trustees had acted negligently. That was to be determined by reference to the standards of the reasonable prudent man of business acting in his own affairs.[22] It was not to be subjectively assessed according to the standard that the particular trustee employed in the conduct

[15] *Mendes v Guedalla* (1862) 2 J & H 259, 277; 70 ER 1054, 1061, *per* Page Wood V-C.

[16] Eg, *Challen v Shippam* (1845) 4 Hare 555; 67 ER 768; *Re Dewar* (1854) 54 LJCh 830.

[17] Such as the production of a mortgage deed as proof that an investment of trust money had in fact been made: *Rowland v Witherden* (1851) 3 Mac & G 568; 42 ER 379.

[18] Eg, *Moyle v Moyle* (1831) 2 Russ & M 710; 39 ER 565 (executors liable for leaving a sum uninvested for some time with a bank which then failed); *Mathew v Brise* (1845) 15 LJCh 39 (Exchequer bills left in the possession of bankers for over a year); *Wyman v Paterson* [1900] AC 271 (proceeds of a bond left in the hands of a law agent for over six months). Cf *Johnson v Newton* (1853) 11 Hare 160; 68 ER 1230 (no breach of trust where money was quite properly left on deposit with a bank which then failed).

[19] Eg, *Hanbury v Kirkland* (1829) 3 Sim 265; 57 ER 998 (without making any inquiries, trustees executed a power of attorney to sell stock so as to enable the other trustee to make an investment on mortgage); *Challen v Shippam*, above (trustees deposited money with bankers, instructing them to invest it in consols, but took no steps for five months to see whether they had done so); *Rowland v Witherden* (1851) 3 Mac & G 568; 42 ER 379 (trustees sold stock and gave the proceeds to a solicitor to invest on mortgage but took no steps whatever to ascertain whether any mortgage was in fact executed); *Cann v Cann* (1884) 51 LT 770 (trustees held liable when they left money on deposit with a bank for fourteen months while seeking a suitable mortgage and the bank then failed).

[20] (1840) 5 My & Cr 178, 214; 41 ER 338, 352.

[21] The usual ones were (i) the manner in which the trustees might have been anticipated to conduct their own affairs: eg, *Moyle v Moyle* (1831) 2 Russ & M 710, 715; 39 ER 565, 567; *Speight v Gaunt* (1883) 9 App Cas 1, 33; or (ii) the conduct of "ordinary men of business": *Speight v Gaunt*, above, at p 20, *per* Lord Blackburn.

[22] *Speight v Gaunt* (1882) 22 ChD 727, 739 (Jessel MR, CA).

of his or her own private affairs.[23] The courts explicitly rejected the view that "whatever is usual may be done by a trustee, whether it is prudent or not".[24]

Exclusion of liability and the meaning of "wilful default"

Lord St Leonards' Act 1859

4.6 It became normal for trust deeds to contain provisions which, at least on their face, appeared to limit the liability of trustees for the acts of their agents. So common were they, that a clause of this kind was implied by one of the first statutory default provisions applicable to trustees - section 31 of Lord St Leonards' Act of 1859.[25] In a somewhat modernised form, it is now section 30(1) of the Trustee Act 1925.[26] As originally enacted, the section provided that the following clause was to be implied into every trust instrument[27]—

> that the Trustees or Trustee for the Time being... shall be respectively chargeable only for such Monies, Stock, Funds, and Securities as they shall respectively actually receive notwithstanding their respectively signing any Receipt for the sake of Conformity, and shall be answerable and accountable only for their Acts, Receipts, Neglects, or Defaults, and not for those of each other, nor for any Banker, Broker, or other Person with whom any Trust Monies or Securities may be deposited, nor for the Insufficiency or Deficiency of any Stocks, Funds, or Securities, nor for any other Loss, unless the same shall happen through their own wilful Default respectively...

4.7 According to Lord Selborne LC in his judgment in *Re Brier*,[28] this section—

> incorporated, generally, into instruments creating trusts the common indemnity clause which was usually inserted in such instruments.[29] It does not substantially alter the law as it was administered by Courts of Equity, but gives it the authority and force of statute law, and appears to me to throw the *onus probandi* on those who seek to charge an executor or trustee with a loss arising from the default of an agent, when the propriety of employing an agent has been established.

4.8 What this passage plainly suggests therefore is that the section—

(1) was merely declaratory of the law;

[23] *Knox v Mackinnon* (1880) 13 App Cas 753, 766; *Rae v Meek* (1889) 14 App Cas 558, 570.

[24] *Bullock v Bullock* (1886) 56 LJCh 221, 224, *per* Kekewich J.

[25] Law of Property and Trustees Relief Amendment Act 1859, 22 & 23 Vict c 35.

[26] For Trustee Act 1925, s 30(1), see Appendix A and, for discussion, below, paras 4.27, 4.38 and 4.45.

[27] The implication was however "without Prejudice to the Clauses actually contained therein".

[28] (1884) 26 ChD 238, 243.

[29] The authorities show that this is is correct. For cases where an express clause in this form was in issue, see *Brice v Stokes* (1805) 11 Ves 319; 32 ER 1111; *Mucklow v Fuller* (1821) Jac 198; 37 ER 824.

(2) applied in relation to the *supervision* of agents who had been properly appointed by trustees[30] but who had defaulted; and

(3) clarified where the onus of proof lay in proceedings against those trustees in such circumstances.

4.9 Because trustees were liable for the defaults of an agent properly appointed only if they failed to exercise the care of a reasonable prudent person,[31] it is implicit that the expression "wilful default" in the section meant no more than "breach of duty". This last point is of some importance and is borne out by an analysis of the authorities. A clear case is *Re Chapman*,[32] where trustees had invested on the authorised security of a mortgage and the value of the security had then fallen. Lindley LJ commented that—

> To throw on the trustees the loss sustained by the fall in the value of securities authorised by the trust, wilful default, which includes want of ordinary prudence on the part of the trustees, must be proved...

It is also noteworthy that Lord Eldon LC treated the standard indemnity clause as doing no more than a court of equity would have done in any event.[33] Inferentially this must have meant that a trustee would be liable for a wilful default, but that signified no more than want of ordinary prudence.

4.10 The term "wilful default" has been used in a variety of different situations in the law and its meaning is dependent on its context.[34] It is unnecessary for present purposes to explore all its uses or to analyse any of them in any great detail. Broadly speaking, there was a difference of opinion as to its meaning between courts exercising equity jurisdiction and those on the common law side, a difference that persisted after the Judicature Acts 1873 - 6.

The meaning of "wilful default" in courts of equity

4.11 There were a number of situations in which the concept of "wilful default" was an issue in equity courts. The approach in each of them was to treat as a wilful default any breach of duty - whatever that duty might be - caused by the voluntary act of the party.[35] The first of these has already been explained and requires no further comment. It was the meaning given to the phrase in the standard trustee indemnity clause.[36]

[30] Lord Selborne LC laid some emphasis on the fact that the agent had been properly appointed: *Re Brier*, above, at pp 243, 244.

[31] See above, para 4.2.

[32] [1896] 2 Ch 763, 776. See too *Speight v Gaunt* (1883) 9 App Cas 1, 14 (trustee not liable for wilful default in exercising proper supervision over his agent where his conduct was not negligent).

[33] "[I]n effect this Court infuses such a clause into every Will, though not directed": *Dawson v Clarke* (1811) 18 Ves 247, 254; 34 ER 311, 313.

[34] See John E Stannard's valuable article, "Wilful Default" [1979] Conv 345, on which we have drawn heavily in this section. Cf *Armitage v Nurse*, *The Times*, 31 March 1997, where Millett LJ suggested that "wilful default" had two meanings, "a want of ordinary prudence" and "a deliberate breach of trust" (a transcript was not available at the time of going to press and our comments are based on the draft judgment).

[35] See, eg *Elliott v Turner* (1843) 13 Sim 477, 485, 486; 60 ER 185, 188, 189.

[36] See above, para 4.9.

4.12 Secondly, there was a common-form condition of sale in contracts for the sale of land that provided that if completion should be delayed for any reason other than the wilful default of the vendor, the purchaser was to pay interest on the balance. Such clauses were capable of abuse and did not excite much judicial sympathy.[37] It is not perhaps surprising to find that "wilful default" was defined widely. The expression was taken to mean—

> a conscious abstention by the vendors from doing that which reasonably they ought to have done...[38] neglect to do something which the vendor ought to have done, having regard to his duty to the purchaser.[39]

The word "wilful" implied—

> nothing blameable, but merely that the person of whose action or default the expression is used, is a free agent, and that what has been done arises from the spontaneous action of his will.[40]

As Lindley LJ explained,

> moral delinquency, intentional delay, wilful obstruction on the part of a vendor, may all be absent, and yet there may be wilful default on his part disentitling him to interest...[41]

4.13 This description could be misleading, because although "wilful default" meant no more than a conscious breach of duty, it acquired a narrower technical meaning when used in the context of an obligation to account. The normal connotation of an obligation to account on the basis of "wilful default" was that the person in question was under a duty to account both for the rents and profits actually received, and those that ought to have been received. The courts had on occasions to ensure that these two related meanings of "wilful default" were kept distinct. They made it clear for example that the standard of diligence expected of a vendor of land who remained in possession was not as demanding as that of others who were in analogous positions, such as a mortgagee in possession, or a personal representative in relation to the assets of the deceased.[42] Pending the completion date, a vendor in possession was entitled to the rents and profits of the land because of his or her substantial interest in the property by reason of the unpaid purchase price.[43] Clearly no question could arise in such circumstances as to what he or she ought to have received because that was of concern only to the vendor. Even though the vendor who remained in possession might be

[37] "The vendor knows whether he is fixing a day for completion which is a reasonable time, having regard to the difficulties which he knows he has to deal with, and if there were not some limit put on these clauses, either by construction or by the wording of them, to prevent vendors taking advantage of their own wrong, these clauses would be very oppressive": *Re Woods and Lewis' Contract* [1898] 2 Ch 211, 213, *per* Lindley MR.

[38] *Bennett v Stone* [1903] 1 Ch 509, 515, *per* Vaughan Williams LJ.

[39] *Ibid*, at p 516.

[40] *Re Young and Harston's Contract* (1885) 31 ChD 168, 175, *per* Bowen LJ.

[41] *Re Hetling and Merton's Contract* [1893] 3 Ch 269, 281.

[42] See *Sherwin v Shakspear* (1854) 5 De G M & G 517, 531, 537; 43 ER 970, 976, 978.

[43] If of course the purchase price *had* been paid, the vendor *was* under an obligation to account to the purchaser for the rents and profits received.

obliged to account for the rents and profits received *after* the completion date had passed,[44] there was no obligation to account for rents and profits that he or she *ought* to have received, provided that he or she acted as a prudent owner of the estate would have done.[45]

4.14 Thirdly, where a vendor had contracted to sell land to a purchaser and, as was usually the case, remained in possession pending completion, he or she was under a duty, variously described,[46] to take reasonable care of the property.[47] A failure to observe this duty was regularly characterised as "wilful default".[48]

4.15 There were (and still are) situations in which a court might order an account on the footing of "wilful default". The law is succinctly summarised in the following passage from the leading Australian textbook on equity—

> In cases where a defendant is in legal or physical possession of property in which the plaintiff has an equitable interest, the plaintiff can sometimes obtain a decree that accounts be taken on the basis of wilful default. This means that the defendant must account not only for all receipts and payments actually made by him but also for all moneys which he would have received if he had managed the property prudently. Typical relationships in which accounts are decreed on this footing are *cestui que trust* and trustee, beneficiary and legal personal representative, and mortgagor and mortgagee. In the case of mortgagor and mortgagee the former is always as a matter of course able to obtain a decree on this basis against his mortgagee in possession, even though he does not allege or prove any act of wilful default on the defendant's part... In other cases, the plaintiff, in order to be entitled to accounts on the basis of wilful default, must allege in his pleading and prove at least one example of wilful default on the part of the defendant, even if the pleading contains such an allegation only as the result of an amendment made at the trial.[49]

4.16 In this context, "wilful default" once again meant no more than "some breach of duty".[50] Thus in *Mayer v Murray*,[51] Jessel MR observed that—

> Every mortgagee who sells and receives the purchase-money is liable for wilful default if he does not receive what he might have received by due

[44] The purchaser's correlative duty in such circumstances was to pay interest to the vendor on the outstanding balance of the purchase price.

[45] *Sherwin v Shakspear*, above.

[46] See Alan Dowling, "The Vendor's Duty of Care Between Contract and Completion" [1995] Cambrian LR 33, 34, 35.

[47] See, eg, *Acland v Gaisford* (1816) 2 Madd 28, 32; 56 ER 245, 247.

[48] See *Crosse v Duke of Beaufort* (1851) 5 De G & Sm 7; 64 ER 994; *Phillips v Silvester* (1872) LR 8 Ch App 173; and Alan Dowling, "The Vendor's Duty of Care Between Contract and Completion" [1995] Cambrian LR 33, 39.

[49] Mr Justice R P Meagher, Mr Justice W M C Gummow & J R F Lehane, *Equity: Doctrines and Remedies* (3rd ed 1992) pp 663, 664; para 2506.

[50] *Re Stevens* [1898] 1 Ch 162, 170, *per* Lindley MR (a case on personal representatives).

[51] (1878) 8 ChD 424, 426.

diligence; so is any ordinary trustee.[52]

The conduct that would justify an order for an inquiry as to what *trustees* might have received but for their wilful default, was the commission by them of a passive breach of trust.[53] It was not necessary to show any "conscious wrongdoing" on their part.[54]

The meaning of "wilful default" in courts of law

4.17 The approach of courts of common law to the meaning of wilful default was quite different from courts exercising equitable jurisdiction. The issue first arose in relation to exclusion clauses in contracts of carriage made by railway companies, in which they sought to exclude liability except where the loss arose from the "wilful misconduct" or "wilful default" of their employees. These expressions were given their literal meaning and were taken to imply "something entirely different from negligence, and far beyond it".[55] Although this interpretation tended to be applied to contracts of carriage, there was a short-lived flirtation with it in relation to the condition of sale in contracts for the sale of land, mentioned above,[56] that provided for the payment of interest by the purchaser if completion were delayed for any reason other than the wilful default of the vendor.[57]

"Wilful default" and directors' indemnity clauses

4.18 The interpretation adopted in the cases on contracts of carriage was subsequently applied to indemnity clauses. The first case concerned a clause by which a company undertook to indemnify the trustees of a debenture trust deed against any claims or demands made against them in respect of anything done by them "without their wilful default".[58] Without apparent citation of authority, the Court of Appeal held that "wilful default" meant—

> deliberately and purposely doing something which he knows, when he does

[52] For the obligations of a mortgagee in possession to account, see *Lord Kensington v Bouverie* (1855) 7 De G M & G 134, 157; 44 ER 53, 62; *White v City of London Brewery Co* (1889) 42 ChD 237; *Palk v Mortgage Services Funding Plc* [1993] Ch 330, 338.

[53] Described by Brightman LJ in *Bartlett v Barclays Bank Trust Co Ltd (No 2)* [1980] Ch 515, 546, as "an omission by a trustee to do something which, as a prudent trustee, he ought to have done - as distinct from an active breach of trust, that is to say, doing something which the trustee ought not to have done".

[54] *Ibid*, at p 546.

[55] *Lewis v Great Western Railway Co* (1877) 3 QBD 195, 213, *per* Cotton LJ. See too at pp 206 (Bramwell LJ), 210 (Brett LJ). For similar cases, see *Goldsmith v Great Eastern Railway Co* (1881) 44 LT 181, 182, *per* Lindley J ("it was more like ordinary carelessness than wilful default"); *Graham v Belfast and Northern Counties Railway Co* [1901] 2 IR 13, 19, *per* Johnson J ("misconduct to which the will is party as contradistinguished from accident, and is far beyond any negligence, even gross or culpable negligence"); *Forder v Great Western Railway Co* [1905] 2 KB 532, 535, 536.

[56] Para 4.12.

[57] See the judgments of Lindley and Lopes LJJ in *Re Mayor of London and Tubbs' Contract* [1894] 2 Ch 524. Cf Kay LJ, dissenting, who followed the traditional approach to the meaning of "wilful default". Orthodoxy was restored in these conveyancing cases by the decision of the Court of Appeal in *Bennett v Stone* [1903] 1 Ch 509, but this was overlooked in *Re City Equitable Fire Insurance Co* [1925] Ch 407, 432, 433, 516.

[58] *Re Trusts of Leeds City Brewery Ltd's Debenture Stock Trust Deed* (1923) [1925] Ch 532n.

> it, is a breach of trust, consisting in a failure to perform his duty as trustee.[59]

4.19 This interpretation was applied subsequently by both Romer J and the Court of Appeal in *Re City Equitable Fire Insurance Co Ltd*.[60] This case concerned an indemnity clause which provided that the directors of a company were not accountable for any of their acts or omissions while acting in the execution of their duties except where it was sustained "by their own wilful neglect or default". Although this clause was "substantially a reproduction" of the standard trustee indemnity clause,[61] already explained,[62] it was not given the same meaning. According to Romer J, with whom the Court of Appeal agreed, a person was guilty of a wilful default only if—

> he knows that he is committing, and intends to commit, a breach of duty, or is recklessly careless in the sense of not caring whether his act or omission is or is not a breach of duty.[63]

Romer J referred expressly to Lord Selborne's remarks on the trustee indemnity clause in *Re Brier*,[64] and in particular, to his comment that the clause did little more than state "the existing law in relation to trustees".[65] Romer J considered that this comment was directed not to the meaning of the words "wilful default" but to "the law as to the employment of agents by trustees".[66] No reference was made to *Re Chapman*[67] or to the other equity cases, outlined above,[68] which might have led him to a different conclusion.

THE TRUSTEE ACT 1925 AND ITS INTERPRETATION

Introduction: the four statutory provisions

4.20 There are four statutory provisions contained in the Trustee Act 1925 which are relevant to the standard of care expected of a trustee when appointing and subsequently controlling an agent.[69] In the following paragraphs we explain both these provisions and the judicial gloss that has been placed upon them. There are also two other statutory provisions that require mention. First, there is a specific provision, considered more fully below,[70] that applies to trustees of a pension trust when

[59] *Ibid*, at p 544, *per* Warrington LJ. See too at p 538, *per* Lord Sterndale MR.

[60] [1925] Ch 407.

[61] *Ibid*, p 438, *per* Romer J.

[62] See above, para 4.7.

[63] [1925] Ch 407, 434, approved by Warrington LJ at p 523.

[64] (1884) 26 ChD 238, 243; above, para 4.7.

[65] [1925] Ch 407, 438.

[66] *Ibid*, at p 439.

[67] [1896] 2 Ch 763, 776; above, para 4.9.

[68] See paras 4.11 and following.

[69] Namely, ss 23(1), 23(2), 23(3) and 30(1). The best commentary on these provisions is found in Robert D Carswell, *Trustee Acts (Northern Ireland)* (1964) pp 52 - 58, 66 - 70, discussing the equivalent sections of the Trustee Act (Northern Ireland) 1958, which are similar to but not identical with the English ones. The author is now Lord Chief Justice of Northern Ireland.

[70] See para 4.52.

delegating their investment functions to a fund manager.[71] Secondly, the Stock Exchange (Completion of Bargains) Act 1976[72] protects trustees who, in the exercise of their investment powers, wish to buy or sell securities through a recognised clearing house or its nominee, or the nominee of a recognised investment exchange.[73] Such trustees will not be guilty of a breach of trust by reason only of the fact that they are obliged either—

(1) to pay for the securities before they are transferred; or

(2) to transfer them before they receive payment.[74]

Trustee Act 1925, section 23(1)

4.21 The first statutory provision is section 23(1) of the Trustee Act 1925. It has already been explained that this section extended the circumstances in which trustees might delegate their ministerial functions to cases in which there was no moral necessity. The subsection may also have changed the standard of conduct expected of trustees when appointing agents under the statutory power. This is because it exempts trustees from liability for the defaults of any agent appointed under it if that agent was "employed in good faith". We consider more fully below the manner in which this phrase has been interpreted.[75] However, there is an important preliminary point that needs to be made by way of background to that discussion.

4.22 This is not the only instance in the Trustee Act 1925 where a trustee is rendered immune from liability if he or she has acted "in good faith". Section 15 of the Act, which has its origins in section 37(2) of the Conveyancing and Law of Property Act 1881,[76] gives trustees and personal representatives power to compound liabilities and compromise any claims relating to the trust or estate, "without being responsible for any loss occasioned by any act or thing so done by him or them in good faith".[77] There is some ambiguity as to the meaning of those words in this context. Prior to the 1881 Act, a compromise by trustees or personal representatives would not be regarded as proper if in making it they were guilty of "wilful default", which in this context meant "negligence".[78] In a case which was decided by the Court of Appeal according to the old law but after the enactment of the Conveyancing and Law of Property Act 1881, Jessel MR observed that—

> in future cases of this kind, section 37 of the Conveyancing and Law of Property Act 1881 will have to be considered. It may have a revolutionary

[71] Pensions Act 1995, s 34(4). For the power to delegate investment decisions to a fund manager, see *ibid*, s 34(2), above, para 3.42.

[72] Section 5(1), as amended by the Financial Services Act 1986, s 194(1).

[73] See s 5(2), as inserted by Financial Services Act 1986, s 194(2), and Financial Services Act 1986, Chapter IV and s 207(1).

[74] This provision has the effect of conferring statutory protection on the trustees in the very factual situation that arose in *Speight v Gaunt* (1883) 9 App Cas 1.

[75] See paras 4.34, 4.40.

[76] That section was extended by the Trustee Act 1893, s 21(2). The present section is derived from s 21(2) but is not identical to it.

[77] Those concluding words have remained the same as they were when originally enacted in 1881.

[78] See *Re Owens* (1882) 47 LT 61, 63, 64.

effect on this branch of the law. It looks as if the only question left would be, whether the executors have acted in good faith or not.[79]

4.23 In a subsequent decision on the subsection, *Re Greenwood*,[80] Eve J held that it provided no defence to a case where the loss arose from the inaction of the trustee or personal representative, but only to a mistaken but *bonâ fide* exercise of the statutory power by him or her.[81] In short, honest but perhaps foolish *action* would be excused but not negligent *inaction*.[82] In so far as this decision may shed any light on the meaning of the words "in good faith" in section 23(1) of the Trustee Act 1925, it appears to support a literal interpretation of them.

4.24 There is one point of uncertainty about section 23(1) that appears to have escaped attention. It has been common for some time for trust instruments to confer on trustees wider delegation powers than they would otherwise enjoy under that subsection. In some cases, the trust instrument will also make clear (expressly or impliedly) the standard of care that is expected of the trustees when exercising that power.[83] But what if it does not? Does the standard laid down in section 23(1) of employment in good faith apply, or is it the old common law requirement of reasonable prudence? So far as we aware, there is no authority which provides any guidance on this issue.

Trustee Act 1925, section 23(2)

4.25 Secondly, as regards the delegation of the performance of a trust of foreign property to an agent or attorney under section 23(2) of the Trustee Act 1925, that subsection provides that trustees "shall not, by reason only of their having made such an appointment, be responsible for any loss arising thereby". The subsection gives no guidance as to the standard of care expected of the trustees when selecting or supervising such an agent or attorney.

Trustee Act 1925, section 23(3)

4.26 Thirdly, the specific powers conferred by section 23(3), which permit trustees to employ—

(1) a solicitor to receive and give a discharge for any money, valuable consideration or property on behalf of the trust; or

(2) a banker or solicitor to receive and give a valid discharge for any money

[79] *Ibid*, at p 64.

[80] (1911) 105 LT 509.

[81] *Ibid*, at p 514 ("In determining... whether the conduct of the trustee has or has not been *bonâ fide* in any particular case, the court is bound to have regard to all the circumstances, and if these lead to the conclusion that the loss has arisen from the neglect or carelessness or supineness of the trustee, and not from a mistaken but *bonâ fide* exercise by him of the statutory powers vested in him, then... the case is one outside the sub-section altogether, and in respect of which no relief is thereby afforded to the trustee").

[82] We are respectfully unable to agree with the interpretation given to Eve J's judgment by Gareth Jones in "Delegation by Trustees: A Reappraisal" (1959) 22 MLR 381, 394. Our reading of it suggests that Eve J was drawing a distinction between action and inaction rather than equating good faith with a lack of negligence in the exercise of the power.

[83] See, eg *Steel v Wellcome Custodian Trustees Ltd* [1988] 1 WLR 167, 170, 174; below, para 4.40.

payable under an insurance policy;[84]

are subject to a significant proviso. It is that—

> nothing in this subsection shall exempt a trustee from any liability which he would have incurred if this Act and any enactment replaced by this Act had not been passed, in case he permits any such money, valuable consideration, or property to remain in the hands or under the control of the banker or solicitor for a period longer than is reasonably necessary to enable the banker or solicitor, as the case may be, to pay or transfer the same to the trustee.

The effect of this proviso is necessarily to preserve the equitable obligation on trustees to exercise the care of the reasonable prudent man of business acting in his own affairs.[85]

Trustee Act 1925, section 30(1)

4.27 Fourthly, the Trustee Act 1925 re-enacted the statutory indemnity clause first introduced by Lord St Leonards' Act 1859[86] in the less verbose version of it that had been adopted in section 24 of the Trustee Act 1893. It remained the case that a trustee was not liable for the losses occasioned by the defaults of his or her agents "unless the same happens through his own wilful default".

4.28 The re-enactment of this provision did of course follow shortly after the decision of the Court of Appeal in *Re City Equitable Fire Insurance Co Ltd*.[87] It was not inevitable that the interpretation of the words "wilful default" in that case - to connote a deliberate or reckless breach of duty - would be applied to the statutory trustee indemnity clause for at least two reasons. First, in *Re City Equitable*,[88] Warrington LJ considered that it was misleading to draw an analogy between the liability of trustees and directors:

> In the case of trustees there are certain definite and precise rules of law as to what a trustee may or may not do in the execution of his trust, and it is no answer for a trustee to say, if, for example, he invests the trust property in his hands in a security which the law regards as an unauthorized security: "I honestly believed that I was justified in doing that". No honest belief will justify him in committing that which is a breach of such a rule of law...

The decisions on the meaning of a trustee indemnity clause were therefore no guide to the interpretation of an analogous clause in a company's articles. Secondly, and following from this, it has been explained that there was authority for the view that *any* breach of duty was a "wilful default" for the purposes of the trustee indemnity clause.[89]

[84] See above, para 3.34.

[85] See above, paras 4.4, 4.5.

[86] See above, para 4.6.

[87] [1925] Ch 407; above, para 4.19. The Court of Appeal gave its judgment in July 1924.

[88] [1925] Ch 407, 523, 524.

[89] See *Re Brier* (1884) 26 ChD 238; above, paras 4.7 and following.

However, in the first case on the statutory indemnity clause to be decided after the *City Equitable* decision, the interpretation there given to the words "wilful default" was in fact adopted. In *Re Munton*,[90] where section 24 of the Trustee Act 1893 rather than section 30 of the Trustee Act 1925 was in issue, Astbury J at first instance considered that the wording of the section was "express, and the *City Equitable* case renders its meaning perfectly clear".[91] On appeal, the Court of Appeal affirmed Astbury J's judgment, but did not find it necessary to express an opinion on the point.

Inherent difficulties

4.29 Before examining the authorities on these sections there are two preliminary points of some importance that must be made. First, it should be emphasised that, in considering the liability of trustees for the defaults of their agents, there cannot be a clear demarcation between their initial appointment of that agent and their subsequent supervision of him or her. If an agent defaults almost immediately after the trustees have appointed him or her, the emphasis will necessarily be on whether they exercised the appropriate degree of care in choosing that agent in the first place because no issue of lack of supervision can arise. But in many situations, the matter will not be so clear cut and both the propriety of the appointment and the diligence of the trustees in supervising the agent will be in issue. Prior to 1926, in determining whether the trustees were liable, the same test applied to both functions: had the trustees acted as a reasonable man of business would have done acting in his own affairs? Given the close interrelationship of these two questions, the application of the same test made good practical sense.

4.30 In this context, we note that in its Twenty-third Report,[92] the Law Reform Committee suggested that section 23(1) of the Trustee Act 1925 was concerned with "the trustee's vicarious liability for the misfeasances of his agent, where that agent has not been employed in good faith", whereas section 30(1) was concerned with "the primary liability of the trustee where loss has been caused to the trust fund by the acts of other persons and, had it not been for the trustee's own wilful default, the loss could have been prevented".[93] We would respectfully question whether this analysis is either wholly accurate or particularly helpful. Vicarious liability "is liability falling on one person for the fault of another irrespective of any fault in the first person".[94] A trustee who individually delegates his or her trusts under section 25 of the Trustee Act 1925 is in the true sense vicariously liable for the acts of the delegate.[95] However, where trustees collectively delegate some function under section 23(1), they are not

[90] [1927] 1 Ch 262.

[91] *Ibid*, p 275. He had earlier quoted the relevant excerpt from Warrington LJ's judgment in *Re City Equitable Fire Insurance Co Ltd* [1925] Ch 407, 525, and commented that "I have read the passage representing the general result of the decision, and it seems to me to apply to the present case": [1927] 1 Ch 262, 274. For criticism of *Re Munton*, see Gareth Jones, "Delegation by Trustees: A Reappraisal" (1959) 22 MLR 381, 391.

[92] The Powers and Duties of Trustees (1982) Cmnd 8733, para 4.10.

[93] In other words, liability for wilful default arose where the trustee had "connived at those actions in some way": *ibid*.

[94] C T Emery, "Delegation by Trustees - Reforming the Law" (1983) 133 NLJ 1095.

[95] He or she "shall be liable for the acts or defaults of the donee [of the power of attorney] in the same manner as if they were the acts or defaults of the donor": Trustee Act 1925, s 25(5) (as substituted by the Powers of Attorney Act 1971, s 9); see above para 3.37.

automatically liable for the misdeeds of their agent.[96] If they are held accountable because they improperly appointed an agent, it is because of their own lack of good faith in his or her selection.[97] This is not intrinsically different from their liability for losses that arise because they have subsequently failed to supervise the agent. We would also doubt whether section 30(1) was intended to protect trustees from the acts, neglects and defaults of their agents in all cases except where they had in some way connived at those misdeeds. The history of the subsection suggests that it was not intended to protect trustees in cases where the loss occurred because of their failure to supervise the agent properly even if they were not privy to his or her misconduct.[98]

4.31 The second preliminary point is, that if the four statutory provisions that have been outlined above are examined without regard to any authority as to their meaning, they cannot obviously be reconciled into any coherent code. Indeed, if they are given a literal interpretation, they do not dovetail at all satisfactorily. It comes as no surprise that they have proved to be troublesome.

The decision in Re Vickery

4.32 The leading authority on the meaning of the four provisions is the well-known decision of Maugham J in *Re Vickery*.[99] It is a case that has been both heavily criticised and staunchly defended, though even its critics accept the correctness of the actual result on its facts. The issue was whether the defendant, a somewhat other-worldly executor[100] of a very small estate[101] was guilty of a breach of trust because he permitted a solicitor to retain certain assets of the estate longer than he should have done. He had instructed a local firm of solicitors that had several branches near his home. Some two and a half months after probate had been obtained,[102] the plaintiff, a beneficiary under the deceased's will, informed the defendant that the solicitor in question had, in the recent past, been suspended for assaulting another solicitor. The plaintiff then discovered that the solicitor had on a previous occasion been suspended by The Law Society for five years. Within a week of first learning of the doubts about the solicitor, the defendant began to press him to complete the administration. He continued to press for the work to be done and eventually instructed another solicitor. The original solicitor defaulted after proceedings had been commenced against him.

4.33 Even if the defendant's conduct had been judged by the standard of the reasonable prudent man of business, it is difficult to see how he could have been liable on the facts in relation to either his choice of agent or his subsequent supervision of him. Indeed, Maugham J held that the most that the defendant had been guilty of was an error of

[96] Cf John E Stannard, "Wilful Default" [1979] Conv 345, 351: "[t]here is not a single case under which a trustee has been held to be *vicariously* liable for the acts of others".

[97] See C T Emery, "Delegation by Trustees - Reforming the Law" (1983) 133 NLJ 1095, 1096. The Law Reform Committee's reference to a trustee's "vicarious liability" can be traced back to Gareth Jones, "Delegation by Trustees: A Reappraisal" (1959) 22 MLR 381, 395.

[98] See above, paras 4.7 - 4.9.

[99] [1931] 1 Ch 572.

[100] He "had spent his life as a missionary in the city of London and... was completely ignorant of business affairs": *ibid*, at p 573, *per* Maugham J.

[101] The sum in issue amounted to some £277.

[102] During which period the defendant was very ill.

judgment.[103] However, the case was not decided on that simple basis.[104] Maugham J gave an exposition of what he regarded as being the interrelationship between sections 23(1), 23(3) and 30(1) of the Trustee Act 1925. It is possible to distil four propositions from the judgment.[105]

Proposition 1

4.34 Following the enactment of section 23(1) of the Trustee Act 1925, trustees were not liable for loss due to the appointment of an agent provided that they had acted in good faith.[106] It is clear that, subject to two provisos, Maugham J intended "good faith" to have its ordinary subjective meaning. Those two qualifications were that the trustees should—

(1) use their discretion in selecting an agent; and

(2) only employ an agent to act within the usual course of his or her business.

However, even if the trustees failed to satisfy those two requirements and the trust thereby suffered loss, as a consequence of section 30(1) of the Trustee Act 1925, they would not be liable for breach of trust in many cases unless they had been guilty of "wilful default".[107]

Proposition 2

4.35 The proviso to the specific powers to authorise certain agents to give a valid discharge for trust monies conferred by section 23(3) of the Trustee Act 1925,[108] which expressly preserved the liability of a trustee who allowed any money, valuable consideration or property to remain in the hands or under the control of the agent longer than was reasonably necessary, had no application to delegations made under section 23(1). This was justified on the basis that—

> in many cases where, for example, a banker or other agent is employed by a trustee to receive money, the money cannot at once be conveniently paid to the trustee, but has to be employed by the banker or other agent in a number of other ways.[109]

It is clear from this passage that the protection afforded by section 23(1) to a trustee who appointed an agent in good faith was not spent once the appointment was made,

[103] See [1931] 1 Ch 572, 584, 585.

[104] As it could so easily have been. Cf *Re Chapman* [1896] 2 Ch 763, 776, where Lindley LJ observed that "[t]rustees acting honestly, with ordinary prudence and within the limits of their trust, are not liable for mere errors of judgment".

[105] These are referred to in what follows as "Vickery Proposition 1", "2," "3" or "4" respectively.

[106] See [1931] 1 Ch 572, 581.

[107] See below, para 4.38. This would not be the case in all situations: see below, paras 4.36 and 4.37.

[108] That is the power to employ a solicitor to receive and give a discharge for any money, valuable consideration or property on behalf of the trust, or a banker or solicitor to receive and give a valid discharge for any money payable under an insurance policy: see above, para 4.26.

[109] [1931] 1 Ch 572, 581.

but continued thereafter.

Proposition 3

4.36 The statutory indemnity clause in section 30(1) did not apply to protect a trustee in *all* cases where the trust had suffered loss. Having regard to the wording of the subsection, it was confined to losses which arose from—

(1) a trustee signing receipts for the sake of conformity;

(2) the wrongful acts or defaults of another trustee;

(3) the wrongful acts or defaults of a banker, broker or other agent with whom trust money or securities had been deposited;

(4) the insufficiency or deficiency of securities; or

(5) any analogous loss.[110]

In situations other than these, a trustee could certainly be liable "for honest mistakes either of construction or fact".[111] This was clear from section 61 of the Trustee Act 1925 which conferred a limited power on the court to grant relief against a breach of trust if the trustee acted "honestly and reasonably, and ought fairly to be excused".

4.37 It should be noted that there may be cases where a trustee delegates to an agent under section 23(1) where section 30(1) is inapplicable. This will be the case in relation to many administrative acts, but it may also include cases where the agent receives money other than as a depository for safe keeping. The obvious example is where he or she is to act merely as a "conduit" for trust money that is either to be received from or to be paid over to some third party on behalf of the trust.[112]

Proposition 4

4.38 The phrase "wilful default" in section 30(1) of the Trustee Act 1925 had the meaning given to it in *Re City Equitable Fire Insurance Co*,[113] namely "either a consciousness of negligence or breach of duty, or a recklessness in the performance of a duty".[114] Maugham J specifically concluded that where an executor, such as the defendant, employed a solicitor or other agent to receive money belonging to the estate in reliance upon section 23(1) of the Trustee Act 1925, he was not liable for any loss unless it occurred through his wilful default, so understood.[115] The defendant was not therefore liable.

[110] *Ibid*, at p 582.

[111] *Ibid*.

[112] See Robert D Carswell, *Trustee Acts (Northern Ireland)* (1964) p 55. Some fine distinctions can be imagined in deciding whether a solicitor was a person with whom money "was deposited". It is not at all clear that Maugham J perceived that there might be a distinction between the agent who merely *receives* money and one with whom it is *deposited*: cf para 4.38 below.

[113] [1925] Ch 407; above, para 4.19.

[114] [1931] 1 Ch 572, 584.

[115] *Ibid*, at pp 583, 584.

Reactions to Re Vickery

4.39 *Re Vickery*[116] has provoked strong reactions ever since it was decided.[117] Some writers have taken the view that Maugham J misinterpreted the relevant statutory provisions and could have construed them in such a way as to leave the previous law substantially unchanged.[118] Others have accepted that he construed those provisions correctly,[119] though some go on to criticise the legislation which Maugham J had attempted to rationalise.[120] We consider in turn each of the four Vickery Propositions.

4.40 Vickery Proposition 1[121] has been criticised because it means that a trustee who honestly but negligently delegates some function to an incompetent or dishonest agent, will escape liability.[122] It has been suggested that the words "in good faith" in section 23(1) of the Trustee Act 1925 could be interpreted to mean "in good faith and without negligence".[123] However, not only is the foundation for this approach rather weak,[124] but there is some modern authority which supports the literal subjective approach adopted in *Re Vickery*. In *Steel v Wellcome Custodian Trustees Ltd*,[125] the court's approval was sought for a scheme to extend the investment and delegation powers of the trustees of a large charity. As we have explained,[126] under the scheme the trustees were to have wide powers to delegate and were to be liable if they failed to take reasonable care either in choosing their agents or in fixing or enforcing the terms of their engagement. In approving the scheme, Hoffmann J observed that it—

> does not ... confer that complete exemption from liability (bad faith apart) which the trustees would have enjoyed if the delegation had been within the more restricted terms of section 23(1) [of the Trustee Act 1925].[127]

4.41 Others have taken the view that it is not so much Maugham J's literal interpretation of section 23(1) of the Trustee Act 1925 that is at fault as the drafting of the subsection itself. It has been said that—

[116] [1931] 1 Ch 572.

[117] Contrast the differing views expressed about the case at the time by Harold Potter (1931) 47 LQR 330 and Sir William Holdsworth, *ibid*, at p 463.

[118] See particularly Gareth Jones, "Delegation by Trustees: A Reappraisal" (1959) 22 MLR 381; John E Stannard, "Wilful Default" [1979] Conv 345, 356; David J Hayton, *Underhill and Hayton: Law of Trusts and Trustees* (15th ed 1995) pp 622 - 624.

[119] And in at least one instance have supported it in principle: see Robert Ham, QC, "Trustees' Liability" (1995) 9 TLI 21, 24.

[120] See, eg Sir William Holdsworth (1931) 47 LQR 463.

[121] Above, para 4.34.

[122] Sir William Holdsworth (1931) 47 LQR 463, 464; Gareth Jones, "Delegation by Trustees: A Reappraisal" (1959) 22 MLR 381, 388.

[123] Gareth Jones, *op cit*, at p 394.

[124] It is based upon an interpretation of *Re Greenwood* (1911) 105 LT 509 with which we disagree: see above, para 4.23.

[125] [1988] 1 WLR 167; see above, para 2.44.

[126] See above, para 2.44.

[127] *Ibid*, p 174. He described what was proposed as being "a reasonable compromise" between the strict liability imposed on a trustee who delegated his trusts under Trustee Act 1925, s 25 (see above, para 3.37) and "the complete exemption of section 23(1)": *ibid*, p 174.

> the Legislature has gone too far in whittling away the liabilities of trustees, with the result that, in some respects, the *cestui que trust* is insufficiently protected.[128]

Similarly, the Law Reform Committee considered that the standard of care found in the subsection was "not stringent enough" and that trustees should be expected to exercise reasonable care in ensuring the competence of any agent whom they were minded to employ.[129]

4.42 In two Australian states which have enacted provisions similar to section 23 of the Trustee Act 1925, Vickery Proposition 1 has been reversed. In both Queensland and Western Australia, the closing words of the equivalent subsections provide that the trustees—

> ... shall not be responsible for the default of any such agent employed in good faith *and without negligence*.[130]

4.43 It has been pointed out that if Vickery Proposition 2[131] is correct, section 23(3) of the Trustee Act 1925 "becomes meaningless and unnecessary".[132] No trustee will ever delegate under the specific powers conferred by section 23(3) because they are subject to the proviso that a trustee will be liable for breach of trust if he or she allows any property to remain in the hands or under the control of the agent longer than is reasonably necessary for the agent to transfer it to the trustee. According to *Re Vickery*, the broad power to delegate under section 23(1) is not subject to the same proviso. As that power is wide enough to encompass the specific situations listed in section 23(3), trustees will always delegate under section 23(1) and section 23(3) becomes redundant. It has been suggested that the obvious means of reconciling sections 23(1) and 23(3) is to "construe the words 'in good faith' in section 23(1) so that they limit only the *act* of employment".[133] However, it has already been explained that Maugham J ruled out this interpretation in *Re Vickery*.[134]

4.44 In Northern Ireland, this particular aspect of the reasoning in *Re Vickery* has been reversed by statute.[135] The Trustee Act (Northern Ireland) 1958[136] provides that the equivalents of *both* sections 23(1) and 23(3) of the Trustee Act 1925 are qualified by the proviso that trustees remain liable if they allow an agent to retain trust money or property longer than is reasonably necessary for them to pay or transfer it to the trustees.

[128] Sir William Holdsworth (1931) 47 LQR 463, 465.

[129] 23rd Report, The Powers and Duties of Trustees (1982) Cmnd 8733, para 4.11.

[130] Trusts Act 1973, s 54(1) (Queensland); Trustees Act 1962, s 53(1) (Western Australia) (italics added). For a discussion of the provisions adopted in the various Australian states, see H A J Ford and W A Lee, *Principles of the Law of Trusts* (2nd ed 1990) para 963.

[131] See above, para 4.35.

[132] Harold Potter (1931) 47 LQR 330, 331.

[133] Gareth Jones, "Delegation by Trustees: A Reappraisal" (1959) 22 MLR 381, 389.

[134] [1931] 1 Ch 572, 581; see above, para 4.35.

[135] See Robert D Carswell, *Trustee Acts (Northern Ireland)* (1964) p 57.

[136] Sections 24(1), (5).

4.45 Vickery Propositions 3[137] and 4[138] stand together. Proposition 3 defines when the trustee indemnity clause found in section 30(1) of the Trustee Act 1925 applies, while Proposition 4 defines the extent of the exemption from liability that it confers on trustees. The main criticism that has been levelled against *Re Vickery* is that Maugham J should not have given the words "wilful default" in that subsection the literal meaning that was adopted in *Re City Equitable Fire Insurance Co*.[139] Not only is that interpretation contrary to earlier authority which held that those words meant no more than "breach of duty",[140] but it also sets the obligations of trustees at a much lower level than hitherto, and one that is inappropriate.[141] Furthermore, it is not readily apparent why, in relation to the five particular types of loss to a trust identified by section 30(1),[142] a lower standard of conduct is expected of trustees than it is in relation to their other acts and omissions.[143] However, the authority of Proposition 4 has recently been placed beyond doubt. In *Armitage v Nurse*,[144] Millett LJ commented that—

> [i]n the context of a trustee exclusion clause... such as section 30 of the Trustee Act 1925, [wilful default] means a deliberate breach of trust: *Re Vickery*.[145] The decision has been criticised, but it is in line with earlier authority.[146] Nothing less than conscious and wilful misconduct is sufficient.

4.46 Not only has Maugham J's interpretation of "wilful default" been endorsed by the Court of Appeal, but it has its defenders as a matter of principle. It has been pointed out that it conforms to the ordinary English meaning of the words and, perhaps more compellingly, that if the words do not have their literal meaning, "the exoneration provision is largely if not wholly deprived of any effect".[147]

4.47 One effect of Vickery Propositions 3 and 4 is particularly anomalous. As we have

[137] Above, para 4.36.

[138] Above, para 4.38.

[139] [1925] Ch 407; above, para 4.19.

[140] See, eg, Gareth Jones, "Delegation by Trustees: A Reappraisal" (1959) 22 MLR 381, 392; John E Stannard, "Wilful Default" [1979] Conv 345, 357. For these earlier authorities, see above, paras 4.11 and following.

[141] See Sir William Holdsworth (1931) 47 LQR 463, 465; David J Hayton, "Trustees and the New Financial Services Regime" (1989) 10 Co Law 191, 194.

[142] Vickery Proposition 3, above, para 4.36.

[143] In Queensland, the difficulty has been resolved by the simple expedient of excluding the word "wilful" from the trustee indemnity clause, thereby making it clear that it is inapplicable where the trustee has committed a breach of duty. The Trusts Act 1973, s 71, provides that a trustee shall not be liable for the matters listed in the section unless the loss occurs "through the trustee's own default".

[144] Reported so far only in *The Times*, 31 March 1997. Our comments are based on the draft judgment.

[145] [1931] Ch 572.

[146] Citing *Lewis v Great Western Railway Co* (1877) 3 QBD 195; *Re Trusts of Leeds City Brewery Ltd's Debenture Stock Trust Deed* (1923)[1925] Ch 532n; *Re City Equitable Fire Insurance Co* [1925] Ch 407.

[147] Robert Ham QC, "Trustees' Liability" (1995) 9 TLI 21, 24. But see above, para 4.7.

explained,[148] trustees' exemption from liability except in cases of wilful default will not apply in all cases where they delegate a function under section 23(1), as for example where an agent receives money on behalf of the trust other than as a depository for safe keeping. In some situations, they may be liable for the acts of such an agent although appointed in good faith, where they have subsequently failed to exercise reasonable prudence in supervising him or her. As the dividing line between initial appointment and subsequent supervision is in no sense precise,[149] we can foresee situations in which there could be uncertainty as to the relevant standard by which to judge the trustees' conduct.

Subsequent authority

4.48 There has been comparatively little authority since *Re Vickery*[150] that sheds any further light on the meaning of the statutory delegation provisions or upon the interpretation given to them in that case.[151] There have been two decisions in which a major trust asset consisted of a shareholding in a company and where the trustee's conduct in relation to that company in some way fell short of what was required. In the first of them, *Re Lucking's Will Trust*,[152] the trustee failed to exercise proper control over the managing director. Cross J held the trustee liable, applying the standard in *Speight v Gaunt*[153]—

> a trustee is only bound to conduct the business of the trust in such a way as an ordinary prudent man would conduct a business of his own.[154]

He explicitly rejected the view the trustee was liable only for "wilful default" and distinguished *Re Vickery*—

> I see no reason whatever to think that Maugham J would have considered that a person employed by a trustee to manage a business owned by the trust was a person with whom trust money or securities were deposited within the meaning of section 30 [of the Trustee Act 1925].[155]

In other words, he applied Vickery Proposition 3[156] and thereby obviated the need to consider the meaning of the trustee indemnity clause found in section 30(1).

4.49 In the second decision, *Bartlett v Barclays Bank Trust Co Ltd (Nos 1 & 2)*,[157] a professional trustee corporation failed to take adequate steps to safeguard the interests

[148] Above, paras 4.36 and 4.37.

[149] See above, para 4.29.

[150] [1931] 1 Ch 572.

[151] But note *Armitage v Nurse, The Times*, 31 March 1997; above, para 4.45. That case was concerned with the construction of an express trustee indemnity clause and the permitted scope of such clauses.

[152] [1968] 1 WLR 866, more fully reported at [1967] 3 All ER 726.

[153] (1883) 22 ChD 727 CA; above, para 4.2.

[154] [1968] 1 WLR 866, 874.

[155] *Ibid*.

[156] Above, para 4.36.

[157] [1980] Ch 515.

of the trust because it did not seek sufficient information as to the conduct of the company in which the trust held its shares. This company engaged in certain unsuccessful speculative ventures which the trustee should have taken steps to prevent. Brightman J[158] accepted that, in principle, the duty of a trustee who had a controlling shareholding in a company was to act "in the same manner as a prudent man of business".[159] However, he went on to qualify that general principle by holding that "a higher duty of care is plainly due from someone like a trust corporation which carries on a specialised business of trust management".[160] Such a trustee would be liable for breach of trust if it neglected "to exercise the special care and skill which it professes to have".[161] We consider more fully the standard of care that can reasonably be expected of trustees in considering options for reform in Part VI of this Paper.[162]

ORDERS UNDER CHARITIES ACT 1993, SECTION 26

4.50 We have explained that the Charity Commissioners may make orders under section 26 of the Charities Act 1993, authorising charity trustees of larger charitable trusts to employ a discretionary fund manager.[163] Under the terms of the Model Order which the Commissioners have issued,[164] the trustees have to be satisfied after inquiry that the manager that they appoint is a "proper and competent person to act in that capacity" who is either—

(1) "an individual of repute with at least fifteen years' experience of investment management" who is an authorised person under the Financial Services Act 1986;[165] or

(2) "a company or firm of repute which is an authorised or exempted person" within the Financial Services Act 1986.[166]

This is, in effect, a duty to take reasonable care, but one that is framed by reference to specific criteria.

PENSIONS ACT 1995, SECTION 34

The general rule: no exclusion of liability for negligence by the trustees

4.51 As we have noted, the Pensions Act 1995[167] gives trustees of an occupational pension

[158] Who, by the time he came to deal with the second part of the case, had become Brightman LJ.

[159] [1980] Ch 515, 532.

[160] *Ibid*, at p 534. Cf *Re Waterman's Will Trusts* [1952] 2 All ER 1054, 1055, where Harman J observed, obiter, that "a paid trustee is expected to exercise a higher standard of diligence and knowledge than an unpaid trustee, and... a bank which advertises itself largely in the public Press as taking charge of administrations is under a special duty".

[161] [1980] Ch 515, 534.

[162] See below, para 6.44.

[163] Above, para 3.41.

[164] See (1994) 2 *Decisions of the Charity Commissioners*, p 31, cl 1. For the full text, see Appendix A.

[165] Such as a member of a self-regulatory organisation, or a person recognised by a professional body: see Financial Services Act 1986, Part I, Chapter III.

[166] Exempted persons include an investment exchange and a clearing house: see Financial Services Act 1986, Part I, Chapter IV.

[167] Sections 34(2); 34(5)(b).

scheme the power to delegate the making of any decision about investments to a fund manager.[168] Under the Act it is in general impossible either for the trustees or the fund manager to exclude liability "for breach of an obligation under any rule of law to take care or exercise skill" in the performance of any of their investment functions.[169] However that principle is qualified in a number of respects[170] of which two are relevant to the present discussion.

Exceptions where discretionary fund managers are employed

4.52 First, it is provided that the trustees will not be responsible for any act or default of a fund manager authorised under the Financial Services Act 1986 if they have taken all such steps as are reasonable to satisfy themselves that—

(1) the fund manager has the appropriate knowledge and experience for managing the investments of the scheme; and

(2) he or she is carrying out the work competently and in compliance with the requirements of the Act in relation to the choice of investments.[171]

4.53 Secondly, where trustees have delegated the making of investment decisions to a fund manager outside the United Kingdom,[172] their liability may be excluded or restricted, but only where they have taken the same steps in relation to the appointment and supervision of that fund manager as they would as regards a fund manager employed in the United Kingdom.[173]

Vicarious liability where there is delegation to some of the trustees

4.54 Where pension trustees have delegated any discretion to make any decision about investments to two or more of their own number, they are vicariously liable for the acts or defaults of those delegated trustees.[174]

[168] See above, para 3.42. This power applies both to fund managers authorised under the Financial Services Act 1986 (as regards business transacted in the UK) and to those operating outside the UK (in relation to business undertaken elsewhere).

[169] Pensions Act 1995, s 33(1).

[170] For further exceptions, see *ibid*, s 33(3).

[171] Pensions Act 1995, s 34(4). For the principles governing the choice of investment, see *ibid*, s 36.

[172] See Pensions Act 1995, s 34(5)(b).

[173] *Ibid*, s 34(6).

[174] *Ibid*, s 34(5).

PART V
TRUSTEES' POWERS OF DELEGATION - A CRITICAL SUMMARY OF THE PRESENT LAW

INTRODUCTION

5.1 In this Part we summarise the main features of the present law on collective delegation by trustees and comment critically on its shortcomings. In the first section we consider the existing powers of delegation that trustees have in the absence of any provision in the instrument creating the trust.[1] We set out the difficulties that the restricted nature of these powers now creates.[2] We suggest that the present characterisation of—

(1) powers of investment; and

(2) some powers of management;

as in all respects fiduciary (and therefore wholly non-delegable) is outmoded.[3] In the second section, we give a critical summary and appraisal of the duties that are presently imposed on trustees when exercising their powers of delegation.[4]

POWERS OF DELEGATION

The present law and its practical consequences

5.2 The essence of the present law is that it permits trustees to delegate their ministerial functions, whether or not there is any necessity for them to do so.[5] They may employ an agent to transact any business or to do any act that is required to be transacted or done in the administration of the trust or of a deceased's estate, whether or not the matter is one which the trustees could themselves have carried out.[6] The deficiencies of the present law are not as to *when* trustees may delegate, but as to *what* they may delegate. Certain limitations on trustees' powers of delegation are wholly appropriate, particularly the requirement that the act delegated must be one which is required to be transacted or done.[7] However, other restrictions now constitute a serious impediment to the proper administration of the trust.

5.3 First, the law does not permit trustees to delegate their trusts and powers collectively

[1] See below, para 5.2.

[2] See below, paras 5.3 - 5.6.

[3] See below, paras 5.10 - 5.15.

[4] See below, paras 5.17 and following.

[5] Trustee Act 1925, s 23(1); above, paras 3.18, 3.19. For the special position of some charity trustees, see above, para 3.41. For the wider delegation powers of pension trustees in matters of investment, see above, para 3.42.

[6] *Ibid.*

[7] Trustee Act 1925, s 23(1); above, para 3.22.

except in relation to trust property[8] which is situated outside the United Kingdom.[9] Some of the difficulties that now arise from the absence of such a power have been explained in Part II of this Paper. In particular, it means that many trustees cannot employ discretionary fund managers.[10] There may even be a doubt as to whether trustees can grant either leases containing rent review clauses or options to sell at a valuation.[11]

5.4 To attempt to meet this difficulty, some trustees now employ the power conferred by section 25 of the Trustee Act 1925.[12] This permits them to delegate their trusts, powers and discretions on an individual basis. If each of them exercises the power, they can, in effect, collectively delegate their fiduciary discretions. However, not only is this practice administratively inconvenient,[13] but it involves the use of this power of delegation for a purpose quite alien to its intended purpose.[14] Furthermore, precisely because the power conferred by section 25 was meant to cover a very different situation, it has two particular consequences that make it unsuitable as a method of collective delegation to agents. First, it does not appear to authorise trustees to remunerate any delegate.[15] Secondly, a trustee who delegates under the section is vicariously liable for the acts or defaults of the delegate.[16] For all of these reasons, there must be some doubt as to whether trustees can safely have recourse to section 25 to enable them to employ discretionary fund managers.[17]

5.5 Secondly, although trustees can delegate their ministerial functions, they have no power to authorise their agents to sub-delegate those tasks, except in relation to trust property abroad.[18] There is an express statutory prohibition on any sub-delegation where a trustee delegates his or her trusts, powers and discretions under section 25 of the Trustee Act 1925.[19] This is another significant impediment to the employment of a discretionary fund manager: as we have already explained, under the the terms of many fund management agreements, a fund manager is authorised to sub-delegate all of its functions to an associate and some to an agent.[20]

5.6 Thirdly, there is considerable uncertainty as to whether trustees can authorise their

[8] Or property which forms part of a deceased's estate.

[9] Trustee Act 1925, s 23(2); above, para 3.20.

[10] See above, para 2.23.

[11] See paras 2.39 and following.

[12] See above, para 3.35.

[13] See above, para 3.37(1) and (4).

[14] See above, paras 3.35, 3.37(2) and 3.38.

[15] See above, paras 3.35, 3.37(6).

[16] Section 25(5); above, para 3.37(5).

[17] If the doubts mentioned in the previous paragraph as to whether trustees can either grant leases containing rent review clauses or options to sell at a valuation are well-founded (and we do not think they are), trustees who were prepared to risk using the power under s 25 would, presumably, have to delegate their power to set a rental or fix a price to the valuer. Each of them would have to execute a power of attorney.

[18] See above, para 3.21.

[19] Section 25(6); above, para 3.37(7).

[20] See, eg IFMA Terms, Cl 6; above, paras 2.21(4), 2.23.

agents to act in ways in which the trustees themselves could not. In particular, it is not clear whether trustees can sanction in advance what would otherwise be breaches of fiduciary duty.[21] Once again, this may be a barrier to employing a discretionary fund manager, because the terms on which it is employed will in many cases require the investor to authorise such conflicts of duty and interest, albeit with safeguards.[22] Whether or not it is desirable that trustees should have such a power is a question of some difficulty,[23] but we consider that it should at least be clarified.

"Delegatus non potest delegare"

5.7 We have seen[24] that the underlying justification for the rule which restricts delegation by trustees is that—

> [a] power involving the exercise of a personal discretion by the donee cannot be delegated: *delegatus non potest delegare*.[25]

The rule encapsulated in this maxim is not confined to trustees, but has been applied to a range of fiduciaries, such as agents[26] and company directors. [27] While it is unnecessary to consider in any detail the application of the maxim to these relationships, the authorities on them - particularly those on the powers of agents - do provide some guidance as to its scope and rationale.

5.8 First, as a general principle, "an agent has no authority to appoint a subagent except with the express or implied authority of the principal".[28] Secondly, where the agent is "selected for some employment, to which peculiar personal skill is essential",[29] or where the principal reposes personal confidence in the agent,[30] that matter cannot be sub-delegated. Thirdly, however, where the task—

(1) "is one which any reasonably competent person can do equally well";[31] or

[21] See above, paras 3.26 - 3.33.

[22] See above, para 2.21(5).

[23] See below, para 6.38.

[24] See above, para 3.3.

[25] C J W Farwell and F K Archer, *Farwell on Powers* (3rd ed 1916) p 499.

[26] *De Bussche v Alt* (1878) 8 ChD 286, 310. See generally F M B Reynolds, *Bowstead and Reynolds on Agency* (16th ed 1996) Chapter 5.

[27] *Re Leeds Banking Co* (1866) LR 1 Ch App 561; *Guinness Plc v Saunders* [1990] 2 AC 663. In practice, this general rule is normally displaced by the articles of association which grant directors express authority to delegate: see Companies (Table A to F) Regulations 1985, 1985 SI No 805, Sched, Table A, art 72. See *Palmer's Company Law* (25th ed 1992) para 8.308.

[28] *John McCann & Co v Pow* [1974] 1 WLR 1643, 1647, *per* Lord Denning MR.

[29] *Burial Board of the Parish of St Margaret Rochester v Thompson* (1871) LR 6 CP 445, 457, *per* Willes J (instancing a painter engaged to paint a portrait). The point in issue in that case was whether a sexton could delegate his tasks of grave digging and bell ringing to a deputy. It was held that he could.

[30] See *De Bussche v Alt* (1878) 8 ChD 286, 310; *Allam & Co Ltd v Europa Poster Services Ltd* [1968] 1 WLR 638, 642.

[31] *Burial Board of the Parish of St Margaret Rochester v Thompson*, above at p 458, *per* Willes J.

(2) although involving a discretion is "a merely ministerial act";[32] or

(3) is one in which no personal confidence is reposed in the agent;[33] or

(4) is such that the "exigencies of business" require it;[34]

a sub-agent can be employed by the agent.[35]

5.9 Agents will of course commonly be employed by the principal under a contract and they will often be engaged precisely because they profess a particular skill. If they consider that they may wish or need to subcontract some part of the work, they can provide for that eventuality in their contract with the principal. The framework within which trustees operate is very different and their scope for restricting the rule more difficult. Their obligations are owed to but are not usually defined by the beneficiaries,[36] but by the terms of the trust. The obligations therefore reflect the actual or (in the case of a trust arising on intestacy) deemed intentions of the settlor. There are of course cases where trustees (like agents) can agree the terms on which they are prepared to act. This will often be the case where the trust authorises the employment of professional trustees.

Should powers of investment and management continue to be regarded as fiduciary?

5.10 We have already briefly considered the underlying principle of *delegatus non potest delegare* as it applies to trustees.[37] We do not seek to question its application in its proper place. In particular, we fully accept "that it makes sense to forbid total delegation of the trust",[38] and that the duty of trustees to distribute the income and the capital of the trust to the beneficiaries or for the objects of the trust[39] is one that should be non-delegable in the absence of express authority in the trust instrument. However, we would take issue with the present law in its characterisation of both the power to select trustee investments and certain powers of management, such as the power to sell, lease or charge trust property, as fiduciary powers for all purposes rather than in part at least as ministerial acts.[40] Decisions of policy may properly be regarded as fiduciary, but their execution within the confines of that policy should not be. Even if

[32] *Ibid*.

[33] *Allam & Co Ltd v Europa Poster Services Ltd*, above at p 642.

[34] *De Bussche v Alt*, above, at p 310, *per curiam*. See, eg, *Re J Mitchell* (1884) 54 LJCh 342 (manager of colliery business for a trust was entitled to employ a solicitor to pay money into court because he could not "be fairly expected to possess the knowledge and skill required to make the payment into Court": *ibid*, at p 345, *per* Chitty J.

[35] For other situations where sub-delegation by agents is permitted, see F M B Reynolds, *Bowstead and Reynolds on Agency* (16th ed 1996) Chapter 5.

[36] Except where the trustees are nominees.

[37] See above, para 3.5.

[38] John H Langbein, "Reversing the Nondelegation Rule of Trust-Investment Law" 59 Mo LR 105, 109 (1994).

[39] Ie, where the trust is a charitable trust or is one of the handful of non-charitable purposes that the law is prepared to countenance. As we explain below, there are considerable difficulties in defining which charitable purposes are delegable and which are not: see para 6.62.

[40] See above, para 3.3.

these powers are to continue to be regarded as being in some sense fiduciary, we consider that the exceptions to the *non delegatus* principle[41] are applicable and justify the delegation of their execution.

5.11 There are two related points about the present characterisation of these powers that are of some significance. First, the fiduciary nature of the power to choose investments was settled at a time when the range of securities in which trustees could invest was exceptionally narrow.[42] The variation of investments was undertaken infrequently and only where a power was expressly or impliedly given for that purpose.[43] It seems curious that a rule that was so conditioned by the circumstances in which it evolved, should have remained both unquestioned and unchanged for so long.[44] Similar considerations apply to other powers of management. The proper administration of a portfolio of leasehold properties or of an agricultural land holding is much more complex than it was when the fiduciary character of certain powers of management was settled. It may nowadays require the regular employment of professional advisers, who may have to make rapid decisions without necessarily being able to refer to the trustees.

5.12 Secondly, in a world in which both investment and property management have become highly skilled tasks, the characterisation of these functions as fiduciary has come to look clumsy and imprecise. This is because it fails to differentiate between two distinct aspects of the investment or management process, namely the policy that trustees adopt and the execution of that policy. A leading authority on fiduciaries, Dr Paul Finn, has identified four duties that are imposed on a fiduciary when exercising a discretion.[45] Those duties are—

(1) not to act for his or her own benefit or for the benefit of any third person;[46]

[41] Outlined above, para 5.8.

[42] Thus in *Robinson v Robinson* (1851) 1 De G M & G 247, 255; 42 ER 547, 550, Lord Cranworth LJ observed that "where trustees have in their hands money which they are bound to secure permanently for the benefit of their *cestuis que trustent*, then, in the absence of express authority or direction to the contrary, they are generally bound to invest the money in the £3 per Cents [ie, Consols]."

[43] A power to vary investments was eventually held to be implied from an express power to invest: *Re Pope's Contract* [1911] 2 Ch 442. It is noteworthy that in that case, Neville J did not consider the point to be free from doubt even then, though there were authorities to the same effect in the late nineteenth century.

[44] Cf *Trustees of the British Museum v Attorney-General* [1984] 1 WLR 418, 424, where Megarry V-C declined to follow cases decided twenty years earlier as to whether the court should confer additional investment powers, because conditions had changed so greatly in that period. "Though authoritative, those cases were authorities only *rebus sic stantibus*; and... they bind no longer".

[45] *Fiduciary Obligations* (1977) Chapter 10. The author is now Mr Justice Finn of the Australian Federal Court.

[46] "[A] person having a power, must execute it *bonâ fide* for the end designed, otherwise it is corrupt and void": *Aleyn v Belchier* (1758) 1 Eden 132, 138; 28 ER 634, 637, *per* Henley LK. See generally, C J W Farwell and F K Archer, *Farwell on Powers* (3rd ed 1916) Chapter 10; P D Finn, *Fiduciary Obligations* (1977) Chapter 11. For an illustration of the rule in relation to powers of management, see *Duchess of Sutherland v Duke of Sutherland* [1893] 3 Ch 169, especially at 187 (life tenant exercised his leasing power to provide a home for his wife: lease set aside). Many such cases will be caught in any event by the rules which preclude a trustee from profiting from his or her fiduciary position.

(2) to treat beneficiaries of the same class equally;[47]

(3) to treat beneficiaries of different classes fairly;[48] and

(4) not to act capriciously or totally unreasonably.[49]

5.13 The management of trust securities or other property can be conducted in accordance with the obligations set out in paragraph 5.12 without it being in any way necessary for the trustees to consider either—

(1) the selection of each investment individually; or

(2) every single exercise of other management discretions such as the selling or leasing of particular parcels of trust property.

What does seem to be required is that the trustees should define the policy within which the management of trust assets is then carried out. That policy *would* of course have to be settled in compliance with the trustees' fiduciary duties that have been outlined in the previous paragraph. The execution of that policy could then be conducted by those with the appropriate professional expertise.

5.14 Four points relating to investment are particularly noteworthy in this context. First, in relation to discretionary fund management, both the IMRO and SFA Rules actually *require* fund managers to conduct investment in accordance with the investment objectives that have been agreed with the client.[50] Secondly, where the courts have sanctioned applications for additional powers to enable trustees to employ discretionary fund managers, they have usually done so on terms that investment is conducted according to policy guidelines laid down by the trustees.[51] Thirdly, when the Charity Commission makes an order extending charity trustees' powers so as to enable them

[47] "[I]t is of the essence of the duty of every trustee to hold an even hand between the parties interested under the trust. Every trustee is in duty bound to look to the interests of all, and not of any particular member or class of members of his *cestuis que trusts*": *Re Tempest* (1866) LR 1 Ch App 485, 487, *per* Turner LJ. See too *Knox v Mackinnon* (1888) 13 App Cas 753 (where trustees favoured one beneficiary as against the others); and *Simpson v Bathurst* (1869) LR 5 Ch App 193 (where the trustee deliberately acted contrary to the interests of one beneficiary).

[48] "[I]t is the duty of trustees to hold a perfectly even hand between all their *cestuis que trust*": *Re Lepine* [1892] 1 Ch 210, 219, *per* Fry LJ. See too *Re Charteris* [1917] 2 Ch 379, 397. The most obvious manifestations of this obligation are certain rather technical rules concerned with maintaining a balance between life tenant and remainderman - *Howe v Earl of Dartmouth* (1802) 7 Ves 137; 32 ER 56; and *Re Earl of Chesterfield's Trusts* (1883) 24 ChD 643.

[49] Where trustees exercise their discretions in good faith, the court will interfere only "where it is mischievously or ruinously exercised" (*Re Brittlebank* (1881) 30 WR 99, 100, *per* Kay J: power of advancement); or where it is exercised "upon unreasonable grounds" (*Lee v Young* (1843) 2 Y & CCC 532, 536; 63 ER 238, 240, *per* Knight Bruce V-C: power to vary securities); or where the trustees' conduct "is so unreasonable as to be vexatious, oppressive, or otherwise wholly unjustifiable" (*Re Chapman* (1895) 72 LT 66, 68, *per* Lindley LJ: trustee unreasonably insisting on evidence of a beneficiary's entitlement, having paid the income to her for 15 years previously). See P D Finn, *Fiduciary Obligations* (1977) Chapter 14.

[50] IMRO Rules, r II-2.4(1)(a); SFA Rules, r 5-23(2) and (4); above, para 2.21(1). See, eg, IFMA Terms, cl 5(a); *ibid*.

[51] See above, paras 2.43; 2.45.

to employ a discretionary fund manager,[52] they will generally do so only on terms that they "lay down a detailed investment policy for the Charity".[53] Finally, under the Pensions Act 1995, where trustees exercise their statutory power to employ a discretionary fund manager,[54] they "must secure that there is prepared, maintained and from time to time revised a written statement of the principles governing decisions about investments for the purposes of the scheme".[55] There are statutory requirements as to what that statement must cover.[56]

5.15 The continuing application of the outmoded rule against delegating discretions in matters of investment and management leads to consequences that are unsatisfactory and irrational. First, although trustees are supposed to make their own selection of investments, albeit after taking advice from an investment adviser, the reality is that they will almost invariably follow that advice while going through the motions of giving it due consideration.[57] Similar considerations no doubt apply to the management of trust property portfolios. This does of course result in practice in "*de facto* delegation".[58] Secondly, there are a variety of collective investment vehicles which are now authorised as trustee investments under the Trustee Investments Act 1961.[59] These are likely to be managed on a discretionary basis by fund managers. Thirdly, we suspect that many trustees simply disregard the restrictions on their delegation powers and act in breach of trust in order to act in what they consider to be the best interests of the beneficiaries.

Summary

5.16 It may therefore be helpful to summarise our conclusions. We consider that there is no longer any continued justification for the existing restrictions on trustees' powers of collective delegation. The principal objection to the present law is that trustees' powers of investment and certain of their powers of management (such as the power to sell, lease or mortgage trust property) are regarded in all respects as fiduciary. As such they must be exercised by the trustees alone and are non-delegable. This position was the product of a time when the decisions which trustees had to take were both comparatively straightforward and infrequent. However, it is increasingly unrealistic, given that many of these tasks (particularly in relation to investment) now arise regularly and often require speedy professional advice and execution. We consider that the "exigencies of business"[60] now justify the delegation of these discretions because adherence to the present restrictions is likely to frustrate the trustees' paramount duty

[52] Under Charities Act 1993, s 26; above, para 3.41.

[53] Model Order, cl 3(b): see (1994) 2 *Decisions of the Charity Commissioners*, p 31.

[54] Section 34(2); above, para 3.42.

[55] Section 35(1).

[56] Sections 35(2), (3); above, para 3.42.

[57] The boundaries between (i) exercise of discretion; (ii) acting under dictation; and (iii) delegating, appear to merge at this point. Cf para 2.18 above.

[58] John H Langbein, "Reversing the Nondelegation Rule of Trust-Investment Law" 59 Mo LR 105, 109 (1994).

[59] See Schedule 1, Part III, paras 3 (authorised unit trusts), 5 (mutual investment societies) and 6 (units of a collective investment scheme). All of these investments were added to the Schedule in or after 1986.

[60] See above, para 5.8.

to act in the best interests of the trust. Trustees should in our view retain their responsibilities for determining investment and management policy in accordance with their fiduciary obligations to act in the best interests of the beneficiaries.

TRUSTEES' DUTIES OF CARE WHEN DELEGATING

Introduction

5.17 As we have explained in Part IV of this Paper, one of the principal criticisms of the statutory default powers of delegation under the Trustee Act 1925 relates to the standard of care expected of trustees when appointing and supervising their agents. Although the criticism has tended to focus on the interpretation given to these statutory provisions[61] in *Re Vickery*,[62] the real difficulty lies in the wording of the provisions themselves, which is such that they do not form a coherent whole. Furthermore, there is a widespread (but by no means universal) feeling that the standards expected of trustees in relation to the appointment and control of their agents is insufficiently demanding, particularly when contrasted with the law prior to 1926.[63]

Summary of the present law

5.18 The present law can be summarised as follows. First, the effect of section 23(1) of the Trustee Act 1925 - both on its literal wording and as it has been judicially interpreted - is that trustees are not liable for a loss which results from the appointment of their agents, provided that they acted in good faith.[64] There is no longer any requirement (as there was before 1926) that they should have acted with reasonable prudence in appointing the agent.

5.19 Secondly, section 23(3) gives trustees a specific power to employ—

(1) a solicitor to receive and give a discharge for any money, valuable consideration or property on behalf of the trust; or

(2) a banker or solicitor to receive and give a valid discharge for any money payable under an insurance policy.

That section preserves the liability of the trustees if they allow any such money, valuable consideration or other property to remain in the agent's hands or under his or her control longer than is necessary.[65] However, this proviso does not affect any delegation made under section 23(1). In consequence, no trustee will ever delegate under section 23(3) as they will be better protected if they appoint under section 23(1).[66]

5.20 Thirdly, by reason of section 30(1) of the Trustee Act 1925, trustees who appoint an agent in good faith under section 23(1) will not in many cases be liable for any loss

[61] Trustee Act 1925, ss 23(1) - 23(3) and 30(1).

[62] [1931] 1 Ch 572; above, para 4.32.

[63] See above, paras 4.38 and following.

[64] See above, paras 4.34 and 4.40.

[65] See above, para 4.25.

[66] See above para 4.35.

subsequently caused by that agent, unless they were guilty of "wilful default".[67] For these purposes, "wilful default" has its literal meaning of a conscious breach of duty or a reckless performance of a duty.[68] There are however some cases of delegation that do not fall within the protection of that subsection, as where an agent is employed simply to transmit trust money or property from one person to another. In such cases a higher standard of conduct is required of the trustees: they will be liable if they should have acted with reasonable prudence.[69] This was the test of liability for trustees in relation to the supervision of their agents prior to 1926. There may therefore be cases where different standards of care apply to the initial appointment of the agent by the trustees (appointment in good faith) and their subsequent control of him or her (acting with reasonable prudence). The difficulty with this state of affairs, is that there is no clear boundary between the trustees' appointment of the agent and their subsequent supervision of him or her.[70]

5.21 Fourthly, it is not clear what standard of care is expected of trustees who appoint agents under an express delegation power in the trust instrument which makes no express or implied provision for the matter.[71] It has never been settled, so far as we are are aware, whether the obligation is to act in good faith or whether the higher standard of reasonable prudence is required.

Orders under the Charities Act 1993, section 26

5.22 In relation to charity trustees, where the Charity Commissioners make an order under section 26 of the Charities Act 1993, authorising the trustees to employ a discretionary fund manager, the trustees are required to satisfy themselves of the standing of that manager and to ensure that he, she or it meets certain specified criteria laid down in the order.[72]

Pension trusts under the Pensions Act 1995, section 34

5.23 Under the provisions of section 34 of the Pensions Act 1995, pension trustees cannot exclude their own liability for negligence.[73] However, they can escape liability for the defaults of any fund manager whom they employ if they comply with specified criteria. Those criteria are, in effect, a code of what constitutes reasonable prudence on the part of the trustees.[74]

[67] See above, para 4.27.

[68] See above, para 4.38.

[69] See above, paras 4.36 and 4.37.

[70] See above, para 4.29.

[71] See above, para 4.24.

[72] See above, para 4.50.

[73] See above, para 4.51.

[74] See above, paras 4.52, 4.53.

PART VI
TRUSTEES' POWERS OF DELEGATION - OPTIONS FOR REFORM

INTRODUCTION

6.1 In this Part we consider how the law on collective delegation by trustees might be reformed and we put forward possible options for consideration. We begin with an examination of and critical commentary upon the views of three other reform bodies[1] - in this country, in Australia and in the United States - which have addressed this issue at various times over the last fifteen years. We take the views of these bodies into account in making provisional proposals for reform.

IS REFORM NEEDED?

6.2 For reasons that we have given in Parts III, IV and V of this Paper, we consider that the present default powers of trustees to delegate their functions to agents are unsatisfactory and that the case for reforming them is overwhelming. First, those powers are no longer wide enough to enable trustees to comply with their paramount obligation to act in the best interests of the beneficiaries. Both the investment of trust assets and the management of trust property now demand specialised skills that many trustees do not have, particularly when they are non-professionals. The present characterisation of both the power of investment and many management powers as fiduciary and wholly non-delegable places trustees in a position where they must act in breach of trust by delegating these discretions to agents if they wish to maximise the potential of the trust assets. Furthermore, the characterisation of trustees' powers of investment and certain of their powers of management as fiduciary dates back to a time when the range of investments was exceptionally limited, and when trustees had the leisure to conduct the affairs of a trust personally.[2] Secondly, the existing statutory provisions which confer the default powers to delegate are badly drafted, and the standard of conduct which they require of trustees when choosing and supervising their agents is widely regarded as insufficiently demanding. **We therefore recommend that the law on trustees' powers of collective delegation should be reformed. We ask readers if they agree. If they do not, we would be grateful if they would explain why they consider that the present law should remain unchanged.**

PREVIOUS LAW REFORM PROPOSALS

The Law Reform Committee's Report on the powers and duties of trustees

6.3 In its Twenty-third Report,[3] the Law Reform Committee considered as part of its review of trustees' powers and duties, their powers of collective delegation.[4] This Report was based on the responses to an earlier consultation paper.

[1] Only one of them on a reference from a particular government.

[2] See above, para 5.16.

[3] The Powers and Duties of Trustees (1982) Cmnd 8733. See above, para 1.12. The Committee's Report arose from a specific reference made to it in 1978 by the then Lord Chancellor.

[4] For a perceptive comment on these proposals, see C T Emery, "Delegation by Trustees - Reforming the Law" (1983) 133 NLJ 1095.

Powers of delegation: the Committee's recommendations

6.4 The Committee considered that trustees' existing powers of delegation under section 23 of the Trustee Act 1925 were adequate and did not need to be widened,[5] commenting that—

> [i]t would not be right to empower trustees to delegate to agents the actual exercise of their discretions. There is a clear distinction between trustees' administrative and managerial functions, which can properly be delegated, and the exercise of their dispositive discretions which cannot under any circumstances be delegated.

It added later in the Report that—

> [n]o general unrestricted power to delegate is either necessary or desirable unless it is bestowed by the conscious decision of the settlor.[6]

6.5 The Committee considered whether there should be an exception to the general rule against delegating discretions to enable trustees to delegate investment decisions.[7] However, it concluded that the power for each trustee to delegate their powers individually under section 25 of the Trustee Act 1925 provided an adequate means of achieving this. Such delegations had to be renewed on an annual basis, which was "a reasonably frequent opportunity to review the exercise of the power".[8] It did however recommend that the doubt as to whether a delegate appointed under section 25 could be paid[9] should be resolved by amending the section, so that trustees could be reimbursed for expenses reasonably incurred in remunerating a delegate employed under the section.[10]

6.6 The Committee also recommended that the scope of section 23(1) should be clarified, so that trustees could only charge the trust fund for the services of agents when those charges had been reasonably incurred.[11] It was concerned to reflect the differences that existed between professional and non-professional trustees. Account would therefore be taken of "the trustee's knowledge, qualifications and experience and the level of remuneration received by him" in determining the reasonableness of those charges.[12]

Powers of delegation: comment

6.7 The responses to the present Paper will reveal whether the view taken by the Law Reform Committee in 1982 that trustees' powers of delegation were adequate still holds good. The strong indications that we have received in preparing it lead us to believe that the opposite view is now widely if not universally held. The fundamental changes that have taken place both in the financial markets and through the

5 *Ibid*, para 4.3. This was the view of a majority of those who had responded on consultation.

6 *Ibid*, para 4.18.

7 *Ibid*, paras 4.16 - 4.20.

8 *Ibid*, para 4.18.

9 See above, para 3.37.

10 The Powers and Duties of Trustees, above, para 4.19.

11 *Ibid*, para 4.6.

12 *Ibid*.

deregulation of residential and agricultural letting since 1982, mean that trusts with investment or property portfolios of any size are likely to require the regular attention of an expert.

6.8 As we have already indicated, we do not believe that the characterisation of either investment or dispositive management powers as fiduciary requires that trustees should be involved in the detailed decision making on a day-to-day basis.[13] In many cases, a trust will, in our view, be better served if the trustees lay down a policy for the investment and management of the trust property in accordance with their fiduciary obligations, leaving the execution of that policy to specialist professionals.[14]

6.9 We have previously explained that a trustee's power to delegate individually his or her discretions under section 25 of the Trustee Act 1925 was never intended to provide a means of employing a fund manager.[15] Nor do we consider that it should be so used. If trustees are to be permitted to delegate their powers of investment and management, it should, in our view, be under a statutory power intended for that purpose.

6.10 As regards the Committee's concern to ensure that professional trustees did not charge twice over for their services,[16] it has in fact now been clearly settled that a trustee's right to be reimbursed from the trust fund in respect of "all expenses incurred in or about the execution of the trusts or powers",[17] is qualified by the requirement that those expenses should have been properly incurred.[18] Indeed this qualification was regarded by the Court of Appeal as being "axiomatic".[19] We do however have much sympathy with the proposal that this requirement of reasonableness should be made statutory, and it is reflected in our own provisional proposals for reform.[20]

6.11 We consider that the fundamental changes that have taken place since 1982 require a substantial widening of trustees' delegation powers. We therefore provisionally reject the Law Reform Committee's recommendation that trustees' powers of collective delegation should remain unchanged, subject only to points of clarification.

Duties of care when delegating: the Committee's recommendations

6.12 We have already explained and expressed our doubts about the Law Reform Committee's analysis of the duties of care expected of trustees under section 23(1) and

[13] See above, paras 5.10 and following.

[14] See above, para 5.13.

[15] See above paras 3.35 - 3.38.

[16] In the United States of America, this practice is known as "double dipping": see John H Langbein, "Reversing the Nondelegation Rule of Trust-Investment Law" 59 Mo LR 105, 108 (1994).

[17] Trustee Act 1925, s 30(2).

[18] *Holding and Management Ltd v Property Holding and Investment Trust Plc* [1989] 1 WLR 1313 at 1324; above, para 3.22. See too Settled Land Act 1925, s 100 ("The trustees of a settlement may reimburse themselves or pay and discharge out of the trust property all expenses properly incurred by them").

[19] *Holding and Management Ltd v Property Holding and Investment Trust Plc*, above, at p 1324, *per* Nicholls LJ.

[20] See below, paras 6.30, 6.34.

30(1) of the Trustee Act 1925.[21] What is of greater importance is the Committee's view that the standard of care expected of trustees when employing an agent under section 23(1) was "not stringent enough".[22] It recommended that section 23(1) should be replaced by a provision to the effect that—

> a trustee shall escape responsibility for the default of his agent only where it was reasonable for him to employ an agent, where he has taken reasonable steps to ensure that the agent employed is competent and where he has taken reasonable steps to ensure that the agent's work has been done competently.[23]

Duties of care when delegating: comment

6.13 It is important to note that the Committee made three recommendations. The second and third of these - that trustees should be expected to exercise reasonable care in selecting and supervising their agents - are considered later in this Part as part of our proposals for reform.[24] The first recommendation does require consideration at this point because it has been criticised.[25] It appears to mark a return to the pre-1926 position, when trustees could only employ agents to perform tasks that they could not reasonably be expected to perform personally.[26] It would be strange to revert to this position at the very time that it is being abandoned in the United States of America because it has proved to be far too constricting.[27] It could also lead to a situation where trustees who chose to delegate a task that they could perform themselves, albeit at their own expense, would become their agent's guarantors. They would therefore be strictly liable for their delegate's defaults, regardless of the care that they may have exercised in choosing and supervising him or her.[28]

6.14 We agree with these criticisms. Given that trustees are only entitled to reimbursement for expenditure reasonably incurred,[29] we see no need to add any further penalty by making them vicariously liable for employing agents when there was no necessity to do so.[30] We therefore provisionally reject the Law Reform Committee's recommendation

[21] See above, para 4.30.

[22] The Powers and Duties of Trustees, above, para 4.11.

[23] *Ibid*.

[24] See below, paras 6.44 and 6.52. The Committee's recommendations on the standard of conduct expected of trustees when delegating should be read in the context of their broader discussion of the standards expected of trustees in the exercise of their powers and duties: see The Powers and Duties of Trustees, above, paras 2.12 - 2.16.

[25] See C T Emery, "Delegation by Trustees - Reforming the Law" (1983) 133 NLJ 1095, 1096.

[26] See above, para 3.8.

[27] "Courts tended to read the requirement... as a prohibition on delegating any function that looked to be important": John H Langbein, "The Uniform Prudent Investor Act and the Future of Trust Investing" 81 Iowa LR 641, 651 (1996).

[28] See C T Emery, "Delegation by Trustees - Reforming the Law", above, at p 1096, who comments that "[i]t is not clear from the Report that the Committee was conscious that it was recommending that a trustee should on occasions be liable for loss to the trust caused by the default of an agent chosen and supervised with exemplary care".

[29] See above, para 6.10.

[30] We do however consider that the concept of reasonable necessity may have a rôle to play in relation to aspects of delegation: see below, paras 6.36, 6.37 and 6.39.

that trustees should only be permitted to delegate when it is reasonably necessary for them to do so. We would however be glad to hear from any reader who disagrees with this view.

The Model Trustee Code for Australian States and Territories

6.15 The Model Trustee Code for Australian States and Territories of 1989,[31] came about as a result of an initiative of a number of distinguished Australian judges, practitioners and academics.[32] The objective was to produce "model clauses together constituting a virtually complete trustee statute, supported by a commentary explaining each clause in detail".[33] It had no official standing, but was intended to provide guidance to any state legislatures that might be interested.[34] The Code contains a power to employ agents in the following terms—

> A trustee may, instead of acting personally, employ and pay an agent to transact any business or do any act required by the trustee to be transacted or done in the execution of the trust or the administration of the trust property, including the receipt and payment of money, the selection and making of investments for the trust, the management of any business and keeping and audit of trust accounts.[35]

In the commentary on this provision, the concern is expressed that "it is beyond a trustee's powers to employ agents to select and make investments for the trust".[36] However, the working party noted that—

> it seems to be regarded as acceptable that trustees should be allowed to employ experts to select and make investments for them, and to do so without necessarily seeking the trustees' approval of a particular course of action before taking it, because the delay involved in obtaining approval might cost the loss of a valuable investment opportunity.[37]

6.16 Specific duties are however imposed on trustees where they employ an agent to select and make investments.[38] It is provided that the trustee—

> (a) shall inform the agent of all the terms and circumstances of the trust that may be relevant to enable the agent to select and make investments suitable for the trust;

[31] It was published by the Law School of the University of Queensland.

[32] The working party that drafted the Code consisted of Meagher J (Supreme Court of NSW); Gummow J (Federal Court of Australia - now High Court); Professor H A J Ford; Dr I Hardingham; Professor P D Finn (now Finn J of the Federal Court of Australia); Legoe J (Supreme Court of SA); Neville Crago; B Ball; and W A Lee.

[33] Preface, p iii. Although the starting point was the existing trustee legislation of the Australian states, there is considerable variation between the provisions of those states.

[34] So far as we are aware, it has not been adopted in whole or part by any state so far.

[35] Cl 3.25(2).

[36] Model Trustee Code, vol 1, p 94.

[37] *Ibid*.

[38] Cl 3.25(4).

(b) shall require him to comply with the provisions if any contained in the trust instrument with respect to the investment of trust funds and otherwise with the law with respect to the investment of trust funds as if the agent were himself a trustee of the trust;

(c) may authorise such agent to select, make and vary investments without prior consultation with the trustee; and

(d) shall require the agent to keep him informed of all investments held, made and varied on behalf of the trustee.

6.17 Provided that they comply with the provisions of the clause, the trustees are exempted from liability for the acts and defaults of their agent unless in employing and supervising him or her they fail to act with an appropriate degree of "care, skill, prudence and diligence".[39] That in turn is determined by reference to "the nature, composition and purposes of the trust" and "the skills which the trustee possesses or ought, by reason of his business or calling, to possess".[40]

Comment

6.18 Those who drafted this provision recognised that it would often be necessary to delegate investment decisions to agents, and they identified a number of reasons for this that we have already noted in Part II of this Paper.[41] By setting out the steps that the trustees must take in delegating such decisions,[42] the clause implicitly distinguishes between the rôle of trustees in determining investment policy and the execution of that policy by an agent. Trustees cannot therefore divest themselves of their fiduciary responsibility for settling that policy. It is by no means clear whether the clause would authorise a similar delegation of management discretions, such as the sale or leasing of trust property. The duty of care that is imposed on trustees when exercising their power to delegate is of particular interest because it recognises that more should be expected both of professional trustees and trustees who have a professional expertise, than from lay trustees.[43]

National Conference of Commissioners on Uniform State Laws: Uniform Prudent Investor Act (USA)

6.19 The Uniform Prudent Investor Act ("UPIA"), which was drafted by the National Conference of Commissioners on Uniform State Laws, was approved by the American Bar Association in February 1995.[44] Its aim is "to update trust investment law in recognition of the alterations that have occurred in investment practice".[45] Although

[39] Cl 3.25(5), referring to cl 1.11.

[40] Cl 1.11. This formulation was chosen in preference to the standard of the "prudent man" because that was thought to be too rigid: see Model Trustee Code, vol 1, pp 24 - 26.

[41] Cf above, para 2.45.

[42] There is, curiously, no requirement for the trustees to review any delegation at regular intervals.

[43] We consider this point further, below, para 6.53.

[44] Although referred to as an "Act" it is of course not so, unless and until a particular state adopts it. Rather, it is declared by the National Conference of Commissioners on Uniform State Laws to be "approved and recommended for enactment in all States".

[45] Prefatory Note, p 1.

its provisions on the delegation of investment and management functions are merely one element of it,[46] they are of considerable significance to the present discussion. This aspect of the UPIA was "presaged" by the American Law Institute's *Restatement of Trusts, Third*, of 1992.[47] Where the *Restatement of Trusts, Second*, of 1959 had adhered to the old orthodoxy that "[t]he trustee is under a duty to the beneficiary not to delegate to others the doing of acts which the trustee can reasonably be required personally to perform",[48] the *Restatement of Trusts, Third*,[49] now states that—

> [a] trustee has a duty personally to perform the responsibilities of trusteeship except as a prudent person might delegate those responsibilities to others. In deciding whether, to whom and in what manner to delegate fiduciary authority in the administration of a trust, and thereafter in supervising agents, the trustee is under a duty to the beneficiaries to exercise fiduciary discretion and to act as a prudent person would act in similar circumstances.

6.20 So far as relevant, section 9 of the UPIA provides that—

> (a) A trustee may delegate investment and management functions that a prudent trustee of comparable skills could properly delegate under the circumstances. The trustee shall exercise reasonable care, skill, and caution in:
>
> (1) selecting an agent;
>
> (2) establishing the scope and terms of the delegation, consistent with the purposes and terms of the trust; and
>
> (3) periodically reviewing the agent's actions in order to monitor the agent's performance and compliance with the terms of the

[46] Its most significant aspect is its adoption of the principle of portfolio theory in relation to investment management. Trustee investment is to be judged by the standard of the prudent investor and in assessing whether trustees have met that standard, regard is to be had to the particular investment "in the context of the trust portfolio as a whole and as a part of an overall investment strategy having risk and return objectives reasonably suited to the trust": UPIA, s 2(b). The are growing signs that portfolio theory is gaining acceptance in this country: see, eg Pensions Act 1995, s 36; and the judgment at first instance of Hoffmann J in *Nestle v National Westminster Bank Plc*, decided in June 1988, reported in (1996) 10 TLI 112, 115 ("[m]odern trustees acting within their investment powers are entitled to be judged by the standards of current portfolio theory, which emphasises the risk level of the entire portfolio rather than the risk attached to each investment taken in isolation"). We are aware that portfolio theory has its critics. We are particularly grateful to Dr Joshua Getzler of St Hugh's College, Oxford, who kindly made available to us his unpublished article, "'Gentlemen Do Not Collect Rents': Fiduciary Obligations and the Problems of Delegation", which contains a very thorough analysis of this criticism. Dr Getzler is also critical of the insistence of English law on strict fiduciary standards from trustees, which he sees as working contrary to the most efficient administration of the trust. We have given his views very careful consideration, but we are aware that he is likely to disagree with much of what we say in this Part.

[47] See John H Langbein, "The Uniform Prudent Investor Act and the Future of Trust Investing" 81 Iowa LR 641, 645 (1996). See too the same author's "Reversing the Nondelegation Rule of Trust-Investment Law" 59 Mo LR 105, 114 (1994).

[48] §171. See above, para 3.4.

[49] §171.

delegation.

(b) In performing a delegated function, an agent owes a duty to the trust to exercise reasonable care to comply with the terms of the delegation.

(c) A trustee who complies with the requirements of subsection (a) is not liable to the beneficiaries or to the trust for the decisions or actions of the agent to whom the function was delegated.[50]

6.21 In their Commentary on the UPIA, the National Conference of Commissioners on Uniform State Laws pinpointed the difficulty of reforming trustees' delegation powers, commenting that—

> [t]here is an intrinsic tension in trust law between granting trustees broad powers that facilitate flexible and efficient trust administration, on the one hand, and protecting trust beneficiaries from the misuse of such powers on the other hand... Delegation, which is a species of trustee power, raises the same tension. If the trustee delegates effectively, the beneficiaries obtain the advantage of the agent's specialized investment skills or whatever other attributes induced the trustee to delegate. But if the trustee delegates to a knave or an incompetent, the delegation can work harm upon the beneficiaries.[51]

Section 9 is, of course, an attempt to strike a balance between "the advantages and the hazards of delegation".[52] It is precisely this tension that any proposal for reform must address.

Comment

6.22 The significance of the UPIA is that it recognises that —

(1) there are now many aspects of both the investment of trust funds and the management of trust assets that it is no longer reasonable to expect trustees to perform personally unless they have particular professional skills in that regard; and

(2) trustees can delegate their discretions in regard to these matters without any abdication of their fiduciary responsibilities to the beneficiaries.

A striking feature of the Act is that it imposes a positive duty on any agent employed by trustees "to exercise reasonable care to comply with the terms of the delegation".[53] English trustee legislation has not of course hitherto proceeded in that way, and we do not consider that it would be appropriate to do so on this occasion. The reforms which we propose are intended to do no more than facilitate the administration of trusts by providing wider default powers for trustees. It is not our intention that they should in some sense be regulatory.

[50] Para (d), which relates to the jurisdiction of state courts is omitted.

[51] Commentary on the Uniform Prudent Investor Act (1995), p 20.

[52] *Ibid*.

[53] Section 9(b).

PROPOSALS FOR REFORM

The issues

6.23 In considering possible options for reform we have of course given careful consideration to these earlier models. We have also paid particular regard to the provisions of the Pensions Act 1995, which permit trustees of a pension trust scheme to delegate their powers of investment,[54] to the practice of the Charity Commissioners when they authorise charity trustees of larger charitable trusts to sanction a similar delegation,[55] and to the decisions of the courts on applications by trustees for additional powers.[56] We do not believe that satisfactory reform can be achieved merely by making amendments to sections 23 and 30 of the Trustee Act 1925. In our view, those provisions should be repealed and replaced by new legislation. We have also been very mindful of the tension between the advantages and the dangers of allowing trustees wide powers of delegation.[57] It should be emphasised that we are recommending what the *default* powers of delegation should be. It would remain open to a settlor (as it is under the present law) to extend or restrict those powers.

6.24 Our proposals address four specific issues—

(1) What powers of delegation should trustees have, and on what conditions, in order to administer the trust in the best interests of the objects of the trust (whether those objects are beneficiaries or purposes)?

(2) Should trustees be given powers to—

(a) authorise sub-delegation by their agents?;

(b) employ agents on terms which limited their liability for their acts as agents?;

(c) sanction possible conflicts of duty and interest by their agents?; or

(d) delegate the performance of any functions to one or more of the trustees?

(3) What standard of care should be expected of trustees when appointing and supervising agents or when delegating to one or more of themselves (whether under any statutory default power or under an express power in the trust instrument)?

(4) To which of the following trusts should any such powers apply—

(a) only trusts created after any legislation came into force?;

(b) to existing trusts as well as new trusts?;

[54] See above, para 3.42.

[55] See above, para 3.41.

[56] See above, para 2.42.

[57] See above, para 6.21.

(c) charitable trusts?; or

(d) pension trusts regulated by the Pensions Act 1995?

What powers of delegation should trustees have?

6.25 We consider that the present distinction between ministerial acts (which can be delegated by trustees) and fiduciary powers (which cannot) should be abandoned. We note that in relation to pension trusts, this distinction has already been abrogated and it has been accepted by Parliament that trustees of an occupational pension trust scheme should have power to delegate investment decisions to a fund manager.[58] We propose that the distinction should in future be between powers to administer the trust and their dispositive powers to distribute trust property for the objects of the trust.[59] The former but not the latter would be delegable by trustees. As we explain below, there are particular difficulties in drawing this distinction in relation to charitable trusts for which we make specific proposals.[60] Our provisional proposals set out below must therefore be read subject to that important caveat. We do not consider that there should be any requirement (as there is in relation to delegations under section 25 of the Trustee Act 1925) that delegation should have to be by power of attorney.[61]

6.26 **Our provisional view is that, subject to any expression of contrary intention in the trust instrument, trustees—**

(1) should have authority to delegate to agents their powers to administer the trust, including their powers of investment and management; but

(2) should have no authority to delegate their powers to distribute the income or capital of the trust for the benefit of its objects, except in relation to trust property abroad.[62]

The power to delegate under (1) could either be in relation to a specific act or acts, or by way of a general retainer. It should remain the case that the matters delegated were ones that were required to be done in the execution of the trust or the administration of a deceased's estate. There should be no requirement that the delegation should be made by power of attorney.

6.27 **These recommendations would be without prejudice to—**

[58] See above, para 3.42.

[59] For this distinction, see Perpetuities and Accumulations Act 1964, s 8(1). Powers of administration are unaffected by the rule against perpetuities, whereas it does affect powers of distribution. In *Pearson v IRC* [1981] AC 753, 774, Viscount Dilhorne, commenting on that subsection, observed that its provisions "show that Parliament distinguished between the administration of a trust and the dispositive powers of trustees and in my opinion there is a very real distinction".

[60] See paras 6.62 - 6.68.

[61] We agree with the comment in the Goode Report, para 4.9.29, that "[i]t does not seem sensible to require trustees who wish to delegate investment management on a discretionary basis to go through all the formalities required for a power of attorney".

[62] We propose that the substance (though probably not the wording) of Trustee Act 1925, s 23(2) should be retained.

(1) the power of an individual trustee to delegate all or any of his or her trusts, powers and discretions under section 25 of the Trustee Act 1925; or

(2) the need to comply with any conditions laid down by law or by the instrument creating the trust in relation to the exercise of any power of investment or management.

6.28 The reason for the first limitation is obvious and it preserves an individual trustee's power to delegate *all* his or her trusts and discretions (including those which are dispositive) in the circumstances for which that statutory power was intended.[63] The second limitation is not strictly necessary because it does no more than state what is already the law. We include it simply to emphasise that trustees cannot escape any preconditions by delegating their powers. It will cover obvious situations such as the following—

(1) where a charity wishes to make a disposition of its property that falls within Part V of the Charities Act 1993 and must comply with certain requirements in relation to such disposition; or

(2) where the consent of some person is required to any disposition of the trust property, whether by the terms of the trust instrument or by statute.[64]

6.29 The wide power of delegation that we propose follows what we understand to have been the usual practice of trust draftsmen for some time, namely to confer beneficial owner powers of delegation on trustees in relation to their investment and management functions.[65] It also follows the model of the UPIA.[66] It does however go beyond the statutory powers of pension trustees under the Pensions Act 1995[67] in that it permits the delegation not only of powers of investment but of powers of management as well.[68] However, not only is the distinction between powers of investment and management an imprecise one,[69] but we can see no good reason for drawing it. **We ask whether readers agree with—**

(1) our proposal for a wider power of delegation and the terms on which it is given; and

[63] See above, para 3.35.

[64] Eg, under Trusts of Land and Appointment of Trustees Act 1996, ss 10, 11.

[65] As we have explained above, para 1.5, the purpose of statutory default powers has traditionally been to imply into trust instruments those provisions normally included by trust draftsmen.

[66] See above, paras 6.20, 6.22.

[67] See above, para 3.42. For our proposals in relation to pension trusts, see below, paras 6.69 and following.

[68] As regards charitable trusts, although the Charity Commissioners are normally asked to extend charity trustees' powers to delegate in relation to matters of investment under Charities Act 1993, s 26, they are in principle willing to give authority in relation to other matters of management that relate to the generation of funds. For s 26, see above, para 3.41. For our proposals in relation to charitable trusts, see below, paras 6.62 and following.

[69] Eg, is the power to purchase land with a view to leasing it a power to invest or a power to manage?

(2) the distinction which it draws between the administration of the trust and the distribution of trust property;

or whether they would prefer some other option.

6.30 The width of our proposed power does of course pose a potential risk to the security of the objects of the trust.[70] It is therefore necessary to have in place proper safeguards for those objects. We have provisionally concluded that there are five safeguards that should be adopted. The first is to prescribe the duty of care to which trustees would be subject when selecting and supervising their agents. We consider what this duty might be below.[71] Secondly, trustees should be required to review any delegation at regular intervals. We do not consider that this would be unreasonably onerous task to impose on trustees because it would only apply to delegations of fiduciary powers which they cannot at present delegate at all in the absence of express authority in the trust instrument. Thirdly, trustees should be under a duty to consider the appropriateness of any delegation of their fiduciary powers before making it. This would involve some form of cost-benefit analysis,[72] and a weighing up of the risks of the proposed delegation against the perceived advantages. The fourth safeguard is built upon the fiduciary obligations to which trustees are subject when administering a trust.[73] In Part V of this Paper we explained our view that trustees' powers of delegation could be widened without abrogating those fiduciary obligations,[74] and we explained that this was already reflected in a number of situations in relation to investment.[75] To this end, trustees who wished to delegate their fiduciary discretions of management and investment would be required both to have and to enforce a written policy which reflected their fiduciary obligations. Finally, we propose to codify the existing law by which trustees are both entitled to recover their own expenditure reasonably incurred in the execution of their duty and to pay their agents reasonable remuneration.[76] The requirement of reasonableness - which (as we have explained) is already the law[77] - would be made explicit by legislation.[78]

6.31 **Our provisional view is that—**

[70] See above, para 6.21.

[71] See para 6.44.

[72] Eg, trustees of a small trust fund would not be justified in appointing a discretionary fund manager if the costs of so doing would be disproportionate to the likely benefits, having regard to alternative investment vehicles available to the fund.

[73] See above, para 5.12.

[74] See above, para 5.13.

[75] See above, para 5.14.

[76] At present, any expenditure properly incurred by the trustees is charged to the capital of the trust fund: see *Re Bennett* [1896] 1 Ch 778. However, the charge is on *both* income and capital so that the trustees are entitled to be reimbursed out of income until provision is made for the sums to be charged to capital: *Stott v Milne* (1884) 25 ChD 710, 715. We would be very interested to know whether any readers consider that trustees should have a power to apportion the expense of employing agents between income and capital, given that both life tenant and remainderman may benefit from the agent's endeavours.

[77] See above, para 6.10.

[78] As we propose the repeal of both sections 23(1) and 30(2) - where, respectively, the trustees' powers to pay agents and to be reimbursed for their expenditure are at present to be found - some statutory provision would be necessary to cover these matters in any event.

(1) trustees should review any delegation of their functions at regular intervals; and

(2) trustees who wished to delegate the powers of management specified in the following paragraph should be required to—

(a) consider the appropriateness of any such delegation before making it;

(b) draw up and review at reasonable intervals a written statement of their policy in relation to the exercise of the powers delegated which reflected their fiduciary obligations to ensure that the trust was administered in the best interests of the objects of that trust;

(c) inform the agent of that policy; and

(d) take reasonable steps to ensure that he or she both complied with it and reported back to the trustees at regular intervals as to its execution.

6.32 **The requirement in paragraph 6.31 would apply to the following powers—**

(1) to select investments;

(2) to sell, lease, or charge trust property;

(3) to grant options or rights of pre-emption over trust property; or

(4) to acquire property for the benefit of the trust.

6.33 We do not wish to impose unnecessary burdens on trustees. It would (for example) be absurd to require them to have a written policy relating to the kinds of ministerial acts that they already have power to delegate under section 23(1) of the Trustee Act 1925. We have therefore confined the written policy requirement to cases where they propose to delegate their fiduciary discretions. It may be that readers will consider that our proposals are either too restrictive or not restrictive enough. **We therefore ask readers whether they agree with our proposals and, in particular, whether they consider that—**

(1) any powers should either be added to or removed from the list in the preceding paragraph; or

(2) any other restrictions or conditions should be imposed.

6.34 **We also propose that the existing statutory provisions that confer powers on trustees to pay agents and to be reimbursed for their own expenses incurred in the execution of their duties[79] should be replaced by a provision that would make it clear that trustees were authorised to pay only the *reasonable* fees of**

[79] See Trustee Act 1925, ss 23(1), 30(2).

their agents and to be reimbursed only for expenditure *reasonably* incurred by themselves. We ask whether readers agree with us.

Specific delegation powers

6.35 There are four particular situations where, if delegation were to be permissible, the degree of risk to the trust would be significantly higher than it is in the ordinary case where trustees employ an agent. The four situations would arise if the trustees—

(1) *appointed an agent and authorised him or her to sub-delegate all or part of the work in question*. We have explained that under the present law, trustees do not have power to contract on this basis.[80] If they did have such a power and exercised it, they would be placing the trust at greater risk than when they employ an agent directly. This is because they would have no control over the sub-agent's selection, terms of appointment and supervision, and because there would be no contractual privity with the sub-agent. The only rights of action that they might have against the sub-delegate in case of default would be either tortious or, if a direct fiduciary relationship could be established,[81] equitable.[82]

(2) *contracted with an agent on terms that limited his or her liability*. It has not been settled whether, under the present law, trustees have power to do this, though our view is that they probably do.[83] The risk in this situation is of course that the trustees might be faced with a loss to the trust from some breach of duty by the agent, but with no rights of recourse against him or her.

(3) *contracted with an agent on terms which sanctioned conduct which would otherwise have involved a conflict of duty and interest*.[84] We have explained that it is uncertain whether trustees may at present contract on this basis.[85] However, this situation is inherently undesirable because it has the potential to remove the protection which equity's strict rules on fiduciaries' conduct provide for the objects of a trust. Those stringent rules prohibiting conflicts of duty and interest by trustees would become meaningless if they could delegate their discretions to an agent who, in performing them, was subject to no similar constraint.

(4) *delegated to one or more of themselves*. Trustees of non-charitable trusts have to act unanimously and exercise their powers jointly. The danger of allowing delegation to just some of the trustees would be that the beneficiaries would lose the protection that this requirement of joint conduct affords. There are particular dangers in allowing delegation to just one trustee, at least where that trustee is not a trust corporation.

Situations (1) and (2)

[80] See above, para 3.21.

[81] See above, para 3.29.

[82] Cf *Henderson v Merrett Syndicates Ltd* [1995] 2 AC 145.

[83] See above, para 3.25.

[84] See above, para 3.27.

[85] See above, para 3.26.

6.36 We consider it likely that trustees will commonly wish to delegate on terms that the agent can sub-delegate or which in some way exclude or restrict the agent's liability. Indeed they may have little alternative in practice but to do so. Our provisional view is that, subject to two safeguards, trustees should have power to delegate on such terms. The first safeguard would be the duty of care which the trustees would owe to the objects of the trust when exercising these powers. We make proposals in relation to this duty below.[86] The second safeguard would be to permit trustees to exercise these powers only if it was reasonably necessary for them to do so, in other words, where a reasonable prudent person would have done the same. We have already explained that we do not agree with the Law Reform Committee's conclusion in its Twenty-third Report,[87] that the requirement of reasonable necessity should be a precondition to *any* delegation by trustees.[88] However, our provisional view is that it *is* a proper requirement to impose in relation to situations (1) and (2). It would compel trustees to examine carefully the terms that were offered to them and to consider what was available from alternative providers of the service in question and on what conditions.

6.37 **We ask whether readers agree with our provisional view that trustees should have power—**

(1) to authorise their agents to employ sub-agents; and

(2) to employ agents on terms which limit their liability;

provided that it was reasonably necessary for the trustees to do so. For these purposes, an act would be reasonably necessary if an ordinary prudent person would have done it.

Situation (3)

6.38 Whether or not trustees should have a power to sanction conflicts of interest on the part of their agents is a question of some difficulty on which we have not formed any definite view. As we have explained—

(1) terms which authorise such conflicts are commonly found in agreements for discretionary fund management;[89] but

(2) it is quite possible for trustees to engage the services of a discretionary fund manager (particularly where the manager is a broker that is neither a market maker nor connected with one) on terms which do not require them to sanction such conflicts.[90]

There may also be situations - such as occurred in *Boardman v Phipps*[91] - where the

[86] See paras 6.44 and following.

[87] The Powers and Duties of Trustees (1982) Cmnd 8733.

[88] See above, para 6.14.

[89] See above, para 2.21(5).

[90] See above, para 2.23.

[91] [1967] 2 AC 46; see above para 3.32.

conduct of the agent, although involving a conflict of duty and interest, may be in the best interests of the trust. One view is that, as what we are proposing is no more than a default power, it should *not* confer on trustees authority to sanction conflicts of interest by agents. If settlors wish their trustees to have such a power, they should confer it expressly. However, although there are likely to be few cases where trustees would feel it either necessary or desirable to contract on such a basis, there could conceivably be some. This is an issue on which the views of readers would be especially welcome, particularly those with practical experience of trust administration. They may feel that, with proper safeguards, such a power poses no real risk to the objects of the trust and that the benefits will substantially outweigh the potential risks. Whichever view readers take, we consider that it would be desirable for the default position to be stated in statutory form.

6.39 **We ask whether readers consider that trustees—**

(1) should not be permitted to sanction actual or potential conflicts of interest by their agents in the absence of express authority in the instrument creating the trust; or

(2) should have power to authorise conflicts of interest by their agents—

(a) if it was reasonably necessary to do so; and/or

(b) if it was it was in the reasonable opinion of the trustees in the best interests of the trust; and/or

(c) in some other circumstances or if some other conditions were satisfied, and if so, what those circumstances or conditions might be.

If readers favour (2), we ask them whether they consider that the requirements in (a), (b) and (c) should be alternative or cumulative.

Situation (4)

6.40 We explained in Part III of this Paper that trustees can probably delegate their *ministerial* functions to one (or presumably more) of their own number as agent of the trust.[92] If they do, then subject to the point explained in the next paragraph, such a delegation appears to be treated in the same manner as if a third party had been appointed as agent by the trustees. We have also noted that, although trustees can delegate their *fiduciary* powers under section 25 of the Trustee Act 1925 to two or more co-trustees, they cannot delegate to a sole co-trustee unless it is a trust corporation as the law stands.[93] If the recommendations which we made in our Report, The Law of Trusts: Delegation by Individual Trustees,[94] are implemented, that particular restriction will be removed. It will then be possible for trustees to delegate their fiduciary powers to just one of their number.

[92] See above, paras 3.14, 3.15.

[93] Section 25(2); above, para 3.35. The trustee who delegates in this way is vicariously liable for the defaults of the delegate: s 25(5); above, para 3.37(5).

[94] (1994) Law Com No 220, paras 4.11 - 4.15. See above, para 3.36.

6.41 The real difficulty about trusts employing one or more of the trustees as agents lies in the issue of remuneration.[95] A leading commentator has observed that—

> [a]s a general rule there is no objection to a fiduciary's doing himself that which he is entitled to employ another to do for reward. A trustee, for example, can act as his own solicitor, or auctioneer. What he cannot do is pay himself for his services without the informed consent of all his beneficiaries.[96]

The reason for this, is that "it is one of the duties of a trustee to take care that no improper charges are made by persons employed for the [trust]".[97] Indeed there is an obvious conflict of duty and interest in allowing payment. However, as we explain in Part X of this Paper, as regards trustees who have professional expertise in the matter in question, this rule has been relaxed by statute in a number of states,[98] and we provisionally propose that the same should be the case in England and Wales.[99] In the light of this and of our earlier provisional recommendations, the obvious (and logical) position to adopt would be to allow trustees to delegate their fiduciary discretions to one or more of the trustees as the agent of the trust.[100] It would still be open to an individual trustee to delegate *all* of his or her trusts and discretion under section 25 of the Trustee Act 1925.

6.42 **Our provisional view is that trustees should be permitted to delegate collectively a function to one or more of their own number whenever they might have delegated it to an agent and subject to the same restrictions. The trustee-agent would be entitled to recover—**

(1) any expenses reasonably incurred in performing the agency; and

(2) if he or she were acting in pursuance of a profession or business, all usual professional or business charges reasonably incurred.

We ask whether readers agree.

6.43 The provisional recommendation in relation to remuneration is subject to two qualifications. The first is that it is contingent on the acceptance of the proposals for an implied professional charging clause that are made in Part X of this Paper.[101] If readers reject those proposals, it would necessarily follow that the trustee-agent would be permitted to recover only his or her expenses. The second concerns the liability of trustees for the conduct of their delegates, where our provisional view is that trustees should be vicariously liable for the acts and defaults of the trustee(s) to whom they

[95] It is undisputed that, where a trustee acts on behalf of the trust, he or she is entitled to be reimbursed for his or her out of pocket expenses: *Re Barber* (1886) 34 ChD 77, 81.

[96] P D Finn, *Fiduciary Obligations* (1977) para 477 (footnotes omitted).

[97] *Broughton v Broughton* (1855) 5 De G M & G 160, 164; 43 ER 831, 833, *per* Lord Cranworth LC.

[98] Including Northern Ireland.

[99] Below, paras 10.26, 10.27.

[100] Under the statutory power that we have proposed above, para 6.26.

[101] See below, paras 10.26 and following.

have delegated their functions. We address this issue below.[102]

Duties of care

Introduction

6.44 As we have endeavoured to show in Part IV of this Paper, the existing rules as to the duties of care expected of trustees when delegating are particularly unsatisfactory. The case for reconsidering them is overwhelming, regardless of any other changes that might be made to the law. There are two principal issues—

(1) in relation to what matters should trustees be required to exercise care when exercising their power of collective delegation?; and

(2) what standard of care should be expected of them?

The first of these matters is more straightforward than the second.

To what matters should the duty of care relate?

6.45 As regards the first of them, we consider that it would be appropriate to follow the model of the UPIA.[103] **Our provisional view is that there should be one standard of care expected of trustees in relation to delegation under the powers which we have proposed and that it should apply to each of the following matters—**

(1) the selection of any agent;

(2) the terms on which the agent is employed; and

(3) the supervision of that agent once appointed.

We ask whether readers agree with this proposal, and if not, what matters they consider should be subject to any duty of care.

What should the standard of care be?

6.46 Our view is that there are five possible standards of care that could be adopted, though our provisional view is that three of these would be inappropriate. We examine each in turn, and then summarise the options for readers to consider.

GOOD FAITH

6.47 The first would be to follow section 23(1) of the Trustee Act 1925 and to continue to employ the standard of good faith. If trustees acted in good faith in relation to the three matters outlined above, they would not be liable for the defaults of their agents. We explained in Part IV of this Paper that this standard has been widely criticised.[104] It does however have its defenders in relation to trustees who are not professional trustees

[102] Para 6.49.

[103] See above, para 6.20.

[104] See above, paras 4.40 and following.

and who have no relevant professional expertise.[105] Although we sympathise with the view that more should be expected of trustees with professional expertise[106] than of lay trustees, we consider that an obligation to act in good faith is not stringent enough to protect the interests of beneficiaries. It is not in our view unreasonable to expect a higher standard than mere good faith even from such lay trustees. As we explain below,[107] a higher standard than mere good faith *is* expected of trustees in relation to the conduct of other aspects of trust business such as investment, and more is expected of professional trustees than of lay ones. We therefore provisionally reject this option.

VICARIOUS LIABILITY

6.48 The second alternative would be to adopt a form of strict liability and to make trustees vicariously liable for the acts of their agents, regardless of the care that they took in selecting and supervising them. This, in our view, would be wholly unreasonable and would be likely to have adverse consequences.[108] First, it would deter persons from acting as trustees. Secondly, if adopted, it would almost certainly impede the proper administration of a trust, because trustees would feel inhibited from delegating in the circumstances in which it was necessary or desirable. We therefore provisionally reject this option as well, subject to one qualification.

6.49 There is, however, a case for imposing vicarious liability in the situation where trustees delegate to one or more of their co-trustees. There are two models for imposing vicarious liability in such a situation. First, where an individual trustee delegates his or her trusts, powers and discretions under section 25 of the Trustee Act 1925, he or she is vicariously liable for the acts of the delegate.[109] If, say, two out of four trustees delegated their trusts to the other two, they would incur the same liabilities for any breach of trust as if they had committed it themselves. Secondly, under the provisions of the Pensions Act 1995,[110] where pension scheme trustees collectively delegate their powers of investment to two or more of their own number, they are vicariously liable for any acts and defaults in the exercise of the discretion. The rationale behind such vicarious liability is obvious: it is a long-established principle of trust law that trustees should be discouraged from any form of "passive delegation".[111] Our provisional view would be to follow the example of these two statutory provisions, and to make all the trustees vicariously liable for the acts and defaults of any trustee(s) to whom they have delegated their functions.

6.50 **We ask readers whether trustees who delegate their discretions to one or more of their own number should be vicariously liable for the acts of the trustee delegates, whatever the standard of care that should otherwise be applicable in relation to powers of delegation.**

[105] See - though not in the context of delegation - Richard Nobles, "Trustees' Exclusion Clauses in Jersey and England" (1996) 10 TLI 66, 68, suggesting that lay trustees should be liable for misinvestment of trust funds only in cases of fraud.

[106] Particularly those who are being remunerated for their services.

[107] Para 6.52.

[108] See, to similar effect, the Goode Report, para 4.9.28.

[109] Section 25(5).

[110] Section 34(5); see above, para 4.54.

[111] See above, para 3.14.

"SAFE HARBOUR" CRITERIA

6.51 The third possible option is to adopt a "safe harbour" test. In other words, a series of criteria would be laid down which trustees would have to satisfy when employing and supervising an agent. If the trustees complied with this "check list", they would escape liability for the acts and defaults of the agent. We are not aware of any existing model for such an approach as regards trustees.[112] The attractions of such an approach are obvious: the trustees know exactly what they must do and that they are immune from risk if they do it. However, while such an approach may be perfectly feasible in relation to specific powers, such as investment, it is impossible to lay down any useful criteria that could apply to all the functions that trustees might wish to delegate. We therefore reject this option.

CONDUCT OF A REASONABLE PRUDENT PERSON

6.52 The fourth option is to adopt the traditional common law rule that "it is the duty of a trustee to conduct the business of the trust with the same care as an ordinary prudent man of business would extend towards his own affairs".[113] There are obvious attractions in adopting this familiar standard.[114] It was the test applicable prior to 1926 in relation to delegation,[115] and it is employed by the UPIA.[116] Furthermore, the standard *may* not be as rigid as it has been perceived to be in other jurisdictions,[117] because it may be a variable and not an absolute one. This is because there may be a gradation as to the standards expected according to whether the trustee is—

(1) an unpaid lay trustee;

(2) a paid professional trustee; or

(3) a professional trustee which holds itself out as such.[118]

[112] Although the Charity Commissioners' Model Order (which indicates the type of conditions that they will impose when authorising the employment of a discretionary fund manager under section 26 of the Charities Act 1993), above, para 4.50, might appear at first sight to provide such a safe harbour approach, it does not. Under the terms of that order, the trustees must be satisfied that the manager is "a proper and competent person to act in that capacity" who fulfils certain specified criteria within the Financial Services Act 1986. However, there is nothing in the Model Order to suggest that compliance with these requirements provides a defence for the trustees should the manager default. The requirements are intended to lay down core standards for the protection of the trust.

[113] *Bartlett v Barclays Bank Trust Co Ltd (No 1)* [1980] Ch 515, 531, *per* Brightman J. Cf the discussion in the Goode Report, para 4.9.7.

[114] It is the standard generally applicable to trustees when conducting the business of the trust: see, eg, in relation to the investment of trust funds, *Re Whiteley* (1886) 33 ChD 347 (CA); (1887) 12 App Cas 727 (HL, *sub nom Learoyd v Whiteley*). It has also been adopted in the Pensions Act 1995, s 34(4) in relation to the delegation of investment decisions to a fund manager, though the provision does not reflect the refinements proposed by the Goode Report, para 4.9.7.

[115] See above, para 4.2.

[116] See above, para 6.20.

[117] See the discussion in the Model Trustee Code for Australian States and Territories (1989), vol 1, pp 24 -26.

[118] See the Law Reform Committee's Twenty-third Report, The Powers and Duties of Trustees (1982) Cmnd 8733, para 2.13.

In the two modern authorities in which this point has been considered, there are suggestions that more is expected of (2) than of (1), and the highest standard of all from (3).[119] The matter is not, however, completely free from doubt.[120]

DUTY OF CARE THAT IS BOTH SUBJECTIVE AND OBJECTIVE

6.53 It has been said that "[t]he main argument against adopting a prudent man rule... is that it infuses a measure of rigidity into an area of the law where flexibility is needed".[121] This led those who drafted the Model Trustee Code for Australian States and Territories to propose instead a requirement that the trustee should—

> act with care, skill, prudence and diligence having regard to—
>
> (a) the nature, composition and purposes of the trust; and
>
> (b) the skills which the trustee possesses or ought, by reason of his business or calling, to possess.[122]

This is of course a refinement of the prudent person test. The duty is defined by regard to—

(1) the characteristics of the particular trust;

(2) the skills which the trustee actually has; or

(3) if he or she is a professional, the skills which the trustee ought to have.[123]

6.54 The final possible option would therefore be to apply a duty of care defined by this more sophisticated standard. The advantage of it lies in its greater flexibility, which

[119] Thus in *Re Waterman's Will Trusts* [1952] 2 All ER 1054, 1055, Harman J commented that "a paid trustee is expected to exercise a higher standard of diligence and knowledge than an unpaid trustee and that a bank which advertises itself largely in the public Press as taking charge of administrations is under a special duty"; and in *Bartlett v Barclays Bank Trust Co Ltd (No 1)*, above, at p 534, Brightman J observed that "a higher duty of care is plainly due from someone like a trust corporation which carries on a specialised business of trust management".

[120] Cf *Jobson v Palmer* [1893] 1 Ch 71, 76, where Romer J considered that there was "no sufficient reason for confining the principle laid down in *Speight v Gaunt* to cases where the trustee is unpaid".

[121] Model Trustee Code for Australian States and Territories, vol 1, p 25.

[122] Section 11.1.

[123] There is an interesting parallel here with the duties owed at common law by a director to a company. In two decisions, Lord Hoffmann has applied a test which looks to the requirements of the particular company, the skills which the director actually has, and those which he or she ought to have: see *Norman v Theodore Goddard* [1991] BCLC 1028, 1030 (as Hoffmann J); *Re D'Jan of London Ltd* [1994] 1 BCLC 561, 563 (as Hoffmann LJ). In each, he accepted that that duty was in fact accurately stated in section 214(4) of the Insolvency Act 1986. It was the conduct of "a reasonably diligent person having both - (*a*) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the same functions as are carried out by that director in relation to the company, and (*b*) the general knowledge, skill and experience that that director has". Cf *Re City Equitable Fire Insurance Co Ltd* [1925] Ch 407, 427 - 429.

enables fuller account to be taken of the attributes of the particular trustee.[124] The issue might not simply be whether the trustee was either paid or held him or herself out as having a particular skill in trust administration in order to secure the trusteeship - which appears to be the two situations in which a higher standard is demanded where the test of reasonable prudence is applied.[125] The conduct of an *unpaid* trustee who had a particular expertise would also be judged according to that skill, and not as if he or she was in all respects a lay person. Furthermore, professional trustees who hold themselves out as having a particular expertise should be judged according to that standard, even if they do not in fact have it. In practice, the difference between the fourth and fifth options may not be very great, and it may be that the common law duty of reasonable prudence is in process of evolving into the standard proposed in the fifth option in any event.

6.55 Our provisional view is that the choice of the relevant standard of care to determine the liability of trustees for the defaults of their agents, lies between the fourth and fifth options, but we would be glad to learn of any other views. **Should the standard of conduct expected of trustees when delegating be that they should—**

(1) act in good faith;

(2) be vicariously liable for all the acts and defaults of their agents;

(3) be required to satisfy a series of specified criteria, compliance with which would be a defence to any proceedings;

(4) be required to act with the care of the ordinary prudent person of business; or

(5) act with the care and diligence that may reasonably be expected having regard to the nature, composition and purposes of the particular trust, the skills which the trustees actually have, or if they are employed as professional trustees, those which they either ought to have or hold themselves out as having?

If any reader favours option (3) we would be grateful for suggestions as to what the criteria might be.

Applicability to express delegation powers

6.56 We have mentioned the uncertainty that exists as to the standard of care expected of trustees when exercising a power to delegate conferred by the trust instrument. **Our provisional view is that the same standard of care that readers select in relation to the proposed statutory power of delegation should apply equally to any express power to delegate conferred by instrument creating the trust unless some other standard is expressly or impliedly specified in that instrument. We ask whether readers agree.**

[124] The court does not take such attributes into account under the common law test of reasonable prudence: see *Learoyd v Whiteley* (1887) 12 App Cas 727, 731, 732.

[125] Cf *Bartlett v Barclays Bank Trust Co Ltd (No 1)* [1980] Ch 515, 534.

To which trusts should any new power of delegation apply?

Introduction

6.57 In this section, we consider the applicability of any new statutory power of delegation of the kind that we have set out. We consider whether it should apply only to trusts created after any legislation was brought into force or to trusts that were already in existence. We also examine the difficulties that exist in seeking to apply the broad new power which we have provisionally proposed to charitable trusts and we make suggestions for their resolution. Finally, we consider the special position of trustees of occupational pension schemes and the interaction of our proposed new power with the overriding power to delegate investment decisions conferred by section 34 of the Pensions Act 1995.

Applicability: general principles

6.58 The Trustee Act 1925 - which contains the present delegation provisions - was applicable to trusts in existence when that Act came into force, except where it was otherwise expressly provided.[126] Our provisional (but strongly held) view is that any new powers of delegation should also apply to existing trusts and not merely to those created after the legislation comes into force. First, as a result of changes in the financial markets in recent years, most professionally drafted trusts will now confer the wide powers that we have proposed. It is existing trusts - and not necessarily ones that are even very old - that are prejudiced by the narrowness of the existing statutory powers of delegation. Secondly, the wider powers proposed will greatly benefit trusts and will enable trustees to administer the trust more effectively in many cases. It could be said that trustees will be prejudiced in one regard. This would be the case if, as we have proposed, a more onerous duty of care were to be imposed upon them when exercising their powers. While we would certainly not belittle that point - we do indeed intend that trustees should be subject to higher duties - we consider that the benefits of wider delegation powers greatly outweigh what to some trustees may be regarded as a drawback. **Subject to what we say in the next paragraph, our provisional view is that any new power of delegation should apply to trusts in existence when any legislation is brought into force as well as to trusts created thereafter. We ask whether readers agree with this view.**

6.59 We have already emphasised that the purpose of having statutory trustee powers is to create a default position that applies in the absence of any expression of contrary intention by a settlor in the trust instrument.[127] Section 69(2) of the Trustee Act 1925 embodies that principle and provides that—

> [t]he powers conferred by this Act on trustees are in addition to the powers conferred by the instrument, if any, creating the trust, but those powers, unless otherwise stated, apply if and so far only as a contrary intention is not expressed in the instrument, if any, creating the trust, and have effect subject to the terms of that instrument.

It has been settled that this subsection has "its exclusive effect if one finds upon a

[126] Section 69(1). There were certain provisions of the Act that were operative only after 1925: see, eg, ss 31 (power of maintenance) and 32 (power of advancement).

[127] See above, para 1.5.

proper reading of the instrument a contrary intention and one need not seek for an express exclusion".[128] It is sufficient if, "on a fair reading of the instrument in question", the application of the particular default statutory power "would be inconsistent with the purport of the instrument".[129]

6.60 As we have indicated, we do not propose to depart from this familiar default approach.[130] Although section 69(2) has generated a certain amount of litigation, it is well known and understood and we consider that the principle that it embodies should apply to any new statutory power of delegation. If the recommendation in the previous paragraph is accepted, the new power would of course be ousted in relation to existing trusts if there was something in the instrument which had created them that was inconsistent with the implication. **Our provisional view is that a provision having the same effect as section 69(2) of the Trustee Act 1925 should apply to any new power of delegation so that it would be inapplicable if a contrary intention was expressed in the instrument creating the trust. We ask whether readers agree with us.**

6.61 There will be some trusts which have applied to the court or to the Charity Commissioners for additional delegation powers.[131] Those powers may be—

(1) less extensive than; or

(2) subject to restrictions which are inapplicable to;

the powers that we propose. It would be unreasonable to expect these trusts to have to incur the trouble and expense of a further application to the court or the Commissioners to bring their powers into line with the new statutory ones, particularly as such an application could hardly be refused. **We provisionally recommend that where a trust has previously been granted additional powers to delegate by the court or the Charity Commissioners, it should have the benefit of the new statutory powers as well. We ask whether readers agree.**

Charitable trusts

THE PARTICULAR PROBLEM

6.62 There is a particular difficulty in applying the proposed new statutory delegation power to charitable trusts.[132] This is for two reasons. First, the concept of "charitable purposes" is in law very much wider than the particular charitable objects for which the trust exists. It is therefore much more difficult to distinguish between those core functions that only the trustees should perform and those which can properly be regarded as delegable. The second reason underlies the first. Powers of delegation that may be appropriate for a non-charitable trust may not be so for a charitable trust. This is because of the special position and privileges enjoyed by charitable trusts in this

[128] *IRC v Bernstein* [1961] Ch 399, 413, *per* Lord Evershed MR.

[129] *Ibid*.

[130] See above, para 1.16.

[131] See above, paras 2.42, 3.41.

[132] We have been greatly assisted on this point by the Charity Commissioners. We are very grateful to them for their helpful advice.

country and the public nature of the needs that they meet. Two points are in our view clear however. First, there are a number of situations in which the administration of many charitable trusts would be greatly facilitated if there were wider default powers of delegation. Secondly, sections 23 and 30 of the Trustee Act 1925 are so unsatisfactory that it would not be appropriate to leave them on the statute book solely to regulate the delegation powers of charity trustees.

6.63 The courts have interpreted very widely what constitutes an application of money for charitable purposes.[133] It has been held to include, in the context of revenue legislation,[134] the donation of funds to another charity,[135] the reinvestment of surplus income,[136] and (probably) payments made for administrative purposes, such as the payment of the salaries of a charity's staff.[137] To prohibit charity trustees from delegating all matters that fall within the umbrella of "charitable purposes" would therefore substantially *narrow* their powers, and would impede rather than assist their functions.

6.64 We have given considerable thought as to how to meet this difficulty, and we have been greatly assisted by advice from the Charity Commissioners. In the following paragraphs we set out our provisional view as to the principles that should govern delegation by charity trustees. We then attempt to translate those principles into proposals for specific delegation powers.

IN WHAT CIRCUMSTANCES SHOULD CHARITY TRUSTEES BE ABLE TO DELEGATE THEIR FUNCTIONS?

6.65 In determining the circumstances in which charity trustees should have power to delegate their functions, we consider that a distinction should be drawn between two aspects of the management of a charitable trust. The first is the generation of income to finance the trust's charitable purposes. The second is the execution of those purposes. **Our provisional view is that charity trustees—**

(1) should have power to delegate matters which relate to income generation even though this entails the delegation of their discretions; but

(2) should have the same powers as they have at present to delegate all other matters relating to the execution of the trusts so that they can only delegate functions which are purely ministerial.

We ask readers whether they agree with our view, and if they do not, what principles they would apply.

[133] See particularly *IRC v Helen Slater Charitable Trust Ltd* [1982] Ch 49.

[134] The relevant statutory provision is now Income and Corporation Taxes Act 1988, s 505(1).

[135] *IRC v Helen Slater Charitable Trust Ltd*, above. For revenue purposes, this particular point has been qualified: see Income and Corporation Taxes Act 1988, s 505(2); Jean Warburton, *Tudor on Charities* (8th ed 1995) pp 286, 287.

[136] *IRC v Helen Slater Charitable Trust Ltd*, above, at p 59.

[137] *Ibid*, pp 55, 56.

THE POWERS PROPOSED

6.66 To meet the difficulties that we have outlined, we have concluded that, instead of giving charity trustees the wide power of delegation that we have proposed for other trustees,[138] they should have a power which specifically lists those functions which they may delegate. Such an approach has obvious dangers - the list may prove to be too wide, too narrow, or insufficiently certain. However it is probably the best that can be done. It also enables some consideration to be given to those functions which charitable trusts should be authorised to delegate in the absence of wider express powers. The Charity Commissioners would of course continue to be able to sanction additional powers if, in a particular case, they were thought to be necessary.[139] We shall be particularly grateful for comments on whether our provisional proposals as to the powers which charity trustees should be permitted to delegate achieves the objectives set out in the previous paragraph.

6.67 **We provisionally recommend that charity trustees should have power to delegate the following functions—**

(1) all matters relating exclusively to the investment of trust property (real or personal), including powers—

(a) to manage such property;

(b) to sell or lease trust property (whether at a fixed price or at a consideration to be fixed by valuation); and

(c) to acquire property for the trust (whether at a fixed price or at a consideration to be fixed by valuation);

(2) all matters relating to the raising of funds for the charity; and

(3) any acts of a ministerial character which are concerned with the administration of the charity;

but no others, unless expressly authorised by the Charity Commissioners. We ask readers to tell us whether they agree with all or any part of this list of functions, and what amendments, additions or deletions they would wish to make to it.

6.68 The powers that we provisionally propose, like the general power that we have set out in relation to all other trusts in paragraph 6.26, could either be exercised in relation to a specific act or acts, or by way of a general retainer. The matters delegated would have to be ones that were required to be done in the execution of the trust, but there should be no requirement that the delegation should be made by power of attorney. The power would be subject to the conditions and rules set out in this Part, except that the requirements set out in paragraph 6.31 would apply only to the powers listed in paragraph 6.67 (1) and (2). If any reader disagrees with this approach, we would be

[138] See above, para 6.26. We have defined these powers both *positively* - to delegate their powers to administer the trust, including their powers of investment and management - and *negatively* - to exclude delegation of the power to distribute trust property for the benefit of the objects.

[139] Charities Act 1993, s 26.

glad to know.

Pension trusts

6.69 Section 34(2) of the Pensions Act 1995 confers on trustees of an occupational pension scheme a power to delegate their discretion to make any decision about investments to a fund manager and prohibits the delegation of such matters in any other way except under section 25 of the Trustee Act.[140] Subject to exceptions that are not here material, those provisions "override any restriction inconsistent with the provisions imposed by any rule of law or by or under any enactment".[141] It follows that this power overrides both section 23 of the Trustee Act 1925, and the common law restrictions on delegating fiduciary discretions. However, as regards the delegation of any other function, pension trustees are subject to same rules as any others. Our provisional view is that, subject to the provisions of the Pensions Act 1995, which would continue to govern the delegation of investment decisions, pension trustees should have the same wide powers of delegation that we have proposed as would all other trustees (other than charity trustees). It may however be that there are special considerations of which we are unaware that apply to pension trusts which mean that a more limited power of delegation would be appropriate. If so, we are anxious to learn of them.

[140] See above, para 3.42.

[141] Pensions Act 1995, s 34(7).

6.70 **We provisionally recommend that, subject to the provisions of the Pensions Act 1995 regarding the delegation of investment decisions, trustees of occupational pension schemes should have the wide powers of delegation proposed in paragraph 6.26, with necessary modifications to take account of the overriding nature of section 34 of the Pensions Act 1995. We ask whether readers agree with us, or whether they consider that there should be restrictions on the powers of such trustees to delegate their non-investment functions, and if so what those might be.**

PART VII
TRUSTEES' POWERS TO EMPLOY NOMINEES AND CUSTODIANS

INTRODUCTION

7.1 In this Part, we examine the limited circumstances in which, in the absence of express powers in the instrument creating the trust, trustees can—

(1) vest trust property in a nominee; or

(2) deposit the documents or other indicia of title with a custodian.

We begin by summarising the present law which is applicable to private trusts and then consider the special situation of charitable trusts.[1] We then summarise why we consider that the law fails to meet the current needs of many trustees and why we think that the law should be changed to give them wide powers to employ nominees and custodians.[2] Finally, we make provisional recommendations that take into account the perceived drawbacks of using nominees that were outlined in Part II of this Paper.[3]

THE PRESENT LAW - PRIVATE TRUSTS

The position at common law

7.2 Three principles underlie the present law—

(1) "The trustee is under a duty to take such steps as are reasonable to secure control of the trust property and to keep control of it".[4] One concomitant of this rule is that trustees cannot make an investment jointly with one or more other persons.[5]

(2) Where there are two or more trustees, it is their duty to ensure that the *title* to the trust property is vested in their joint names, so that it can be transferred

[1] See below, paras 7.2 and following.

[2] See below, paras 7.14 and following.

[3] See below, paras 7.16 and following.

[4] W F Fratcher, *Scott on Trusts* (4th ed 1987) § 175. In *Wyman v Paterson* [1900] AC 271, 288, Lord Davey described it as being "the first duty of the trustees... to preserve the trust fund under their own control". In that case, trustees were held liable for leaving the trust fund in the hands of their law agent for five months. They expected him to deposit the money in his own name and not even in those of the trustees. For other examples see *Mathew v Brise* (1845) 15 LJCh 39 and *Ex p Ogle* (1873) LR 8 Ch App 711. In the former, a trustee invested trust monies in Exchequer bills (which were an authorised investment), but left them in the possession and control of bankers who were thereby able to misappropriate them. The trustee was held to be in breach of trust and had to make restitution to the trust for its loss. In the latter, a trustee in bankruptcy allowed wines and spirits belonging to the bankrupt to remain in the custody of the bankrupt; the wines and spirits were consumed, and the trustee was held liable for the breach of trust in failing to get in the trust property. See too *Salway v Salway* (1831) 2 Russ & M 215, 218; 39 ER 376, 377, 378.

[5] *Webb v Jonas* (1888) 39 ChD 660 (investment in a contributory mortgage together with others a breach of trust).

only with the consent of all.[6]

(3) It is permissible for the *documents* relating to the trust property to be in the custody of just one of the trustees.[7] Although we are not aware of any authority on the point, the same must presumably be true of any chattels held on trust.

7.3 It follows from these principles that, in the absence of either any express power in the trust instrument or any statutory power,[8] trustees cannot vest trust property in nominees or place trust documents in the custody of a custodian. If a trustee places trust property in the hands of a third party when he has no power to do so, he or she will commit a breach of trust[9] and will be liable for any loss that is caused by that breach "however unexpected the result".[10] This is because the normal common law rules of remoteness of damage and causation do not apply to actions for breach of trust. It is enough that there is—

> some causal connection between the breach of trust and the loss to the trust estate for which compensation is recoverable, viz the fact that the loss would not have occurred but for the breach.[11]

Thus even if the actual cause of the breach is the act of some third party - such as the nominee or its agents - the trustees would be liable for the breach of trust.[12] However, as we have already explained—

(1) many nominees and custodians will now be regulated under the Financial Services Act 1986;[13] and

(2) if the loss to the trust was caused by the default of such a person and they had became insolvent, the trustees would have a claim under the Investors Compensation Scheme, though only up to a limit of £48,000.[14]

[6] "The theory of every trust is that the trustees shall not allow the trust moneys to get into the hands of any one of them, but that all shall exercise control over them": *Re Flower and Metropolitan Board of Works* (1884) 27 ChD 592, 596, *per* Kay J. See too *Rodbard v Cooke* (1877) 36 LT 504, 505.Trustees will be liable for a breach of trust if they allow trust property to be vested in the name of just one of their number: *Lewis v Nobbs* (1878) 8 ChD 591.

[7] *Cottam v Eastern Counties Railway Co* (1860) 1 J & H 243; 70 ER 737. There is no requirement therefore that the documents should be deposited with a bank where they are accessible only on the joint application of all the trustees: *Re Sisson's Settlement* [1903] 1 Ch 262.

[8] For statutory powers to employ custodians, see below, paras 7.5 and following.

[9] "[I]f a trustee so deals with a trust fund as to allow a third party to obtain the control over it, whereby it is afterwards lost, he becomes liable for a breach of trust by acting beyond the scope of his authority": *Browne v Butter* (1857) 24 Beav 159, 161, 162; 53 ER 317, 318, *per* Romilly MR.

[10] *Clough v Bond* (1838) 3 My & Cr 490, 496; 40 ER 1016, 1018, *per* Lord Cottenham LC.

[11] *Target Holdings Ltd v Redferns* [1996] AC 421, 434, *per* Lord Browne-Wilkinson.

[12] *Ibid*.

[13] See above, paras 2.9, 2.15. Custody will be regulated where it involves the safeguarding and administering (or arranging for such safeguarding or administering) of another's assets where those include investments: see above, para 2.12.

[14] See above, para 2.11.

7.4 The basis of the general prohibition on trustees employing nominees and custodians lies in the requirement that they must keep the trust assets under their own control. It follows that it cannot be circumvented by the trustees employing the nominee or custodian as agent either under their existing delegation powers[15] or even under the wider powers that we have proposed in Part VI of this Paper.

Statutory exceptions to the common law rule

7.5 There are a number of limited statutory exceptions to the common law rule that bars the employment of nominees and custodians by trustees,[16] and these are explained in the following paragraphs.

Where the trustees act collectively

TRUSTEE ACT 1925, SECTION 21

7.6 First, section 21 of the Trustee Act 1925[17] empowers trustees to deposit any documents held by them relating to the trust, or to the trust property, with any banker or banking company or any other company whose business includes the undertaking of the safe custody of documents. Any fee in respect of such a deposit must be paid for out of income. This power is very limited—

(1) It is confined to *documents* that relate to the trust or to trust property. There is no power to vest *trust property* in a nominee.

(2) The custodian must either be a banker or a company. There is no power to deposit documents with say, a partnership that undertakes the business of custodianship.

(3) There is no power to charge the costs to capital.

TRUSTEE ACT 1925, SECTION 7

7.7 Secondly, under section 7(1) of the Trustee Act 1925,[18] there is a statutory duty on trustees to deposit bearer securities with a banker or banking company for the purposes of safe custody and the collection of income. The trustees are not responsible for any loss incurred by reason of any such deposit.[19] There is no similar statutory duty in respect of any other form of trust property, even though such property might be of considerable value and as readily disposable as bearer securities.

PUBLIC TRUSTEE ACT 1906, SECTION 4

[15] See (1994) 2 *Decisions of the Charity Commissioners*, p 30.

[16] It should also be noted that the Stock Exchange (Completion of Bargains) Act 1976, s 5, as amended by the Financial Services Act 1986, s 194(1), provides that a trustee is not liable for breach of trust merely because he or she parts with the title to securities to a recognised clearing house or its nominee or the nominee of a recognised investment exchange before receiving payment, or makes payment for securities to such a body before obtaining title to them. This is to accommodate normal market dealing. See above, para 4.20.

[17] See Appendix A for the text.

[18] *Ibid*.

[19] Trustee Act 1925, s 7(2).

7.8 Finally, section 4 of the Public Trustee Act 1906[20] confers a power to appoint either the Public Trustee[21] or certain other bodies corporate[22] to act as a custodian trustee.[23] The appointment may be made by—

(1) the court on the application of anyone on whose application it could order the appointment of a new trustee;

(2) the person who created the trust; or

(3) any person having the power to appoint new trustees (which will usually include the trustees).[24]

7.9 When such a trustee is appointed, the trust property is transferred to it as if it were sole trustee, but the management of the trust and the exercise of any power or discretion remains vested in the trustees other than the custodian trustee.[25] It has been said that—

> a trust with custodian and managing trustees is in a class by itself, since it involves a statutory severance, with no counterpart elsewhere, of the functions normally combined in the office of trustee; so that the legal right to the trust property, including the legal right to exercise voting power in respect of shares subject to the trust, is vested in the custodian, whereas all powers of management, including the direction of any exercise of such voting power, are reserved to the managing trustees.[26]

7.10 Although custodian trusteeship offers a number of advantages, particularly in ensuring the security of the trust fund against possible breaches of trust, it "has not... greatly commended itself to the public"[27] and is "very little used at any rate in private trusts".[28] Although until recently this was because there was little demand for such a facility,[29] it has not gained in popularity even though nominees are now widely used in the conduct of investment business. The reason is that custodian trusteeship does not meet that particular need. The requirements of both the Public Trustee Act 1906

[20] See Appendix A for the text.

[21] The Public Trustee cannot accept any trust that is exclusively for religious or charitable purposes: Public Trustee Act 1906, s 2(5). There are no similar limitations on the other bodies which may act as custodian trustees: see *Re Cherry's Trusts* [1914] 1 Ch 83.

[22] For these, see the Public Trustee Rules 1912, SR & O 1912 No 348, r 30 (as amended). The bodies include the Treasury Solicitor and certain corporations constituted under the law of any part of the United Kingdom or the European Union which comply with certain conditions laid down in the rules.

[23] See generally, David J Hayton, *Underhill and Hayton: Law of Trusts and Trustees* (15th ed 1995) pp 774 - 780.

[24] Public Trustee Act 1906, s 4(1).

[25] *Ibid*, s 4(2)(*a*), (*b*), (*d*). All sums payable to or out of the income or capital of the trust property shall be paid to or by the custodian trustee, though he may allow the managing trustees to receive any dividends or other income from the trust property: *ibid*, s 4(2)(*e*).

[26] *IRC v Silverts Ltd* [1951] Ch 521, 530, *per* Evershed MR.

[27] David J Hayton, *Underhill and Hayton: Law of Trusts and Trustees* (15th ed 1995) p 775.

[28] Law Reform Committee, 23rd Report, The Powers and Duties of Trustees (1982) Cmnd 8733, para 4.27.

[29] *Ibid*.

and the Public Trustee Rules 1912 made under it are very prescriptive and confer only limited powers on custodian trustees. As a result they cannot fulfil the rôle that nominees are now expected to perform in the sphere of investment.[30] Furthermore, the types of body that can act as custodian trustees are confined to corporations of a particular kind, such as trust corporations. The nominee companies employed by brokers and banks seldom meet those requirements because they are set up solely to act as nominees and not for any wider purpose. Firms of solicitors or accountants, being partnerships, cannot act as custodian trustees.

Where trustees act individually

TRUSTEE ACT 1925, SECTION 25

7.11 In addition to these powers which must be exercised by the trustees collectively, there is a power for an individual trustee to delegate any of the trusts, powers and discretions vested in him or her under section 25 of the Trustee Act 1925.[31] We have already explained in some detail both the purpose of this section and how it works.[32] As we have seen, if all the trustees are so minded, it is possible, using this section, for each of them to delegate all or some of their powers to a particular person by power of attorney for a period of up to twelve months.[33] However, there must be some doubt whether trustees could use this statutory power to vest trust property in a nominee. As the basis of the prohibition on the use of nominees by trustees is not the rule against the delegation by them of their trusts and fiduciary discretions but their obligation to keep the trust property under their control,[34] it is at least arguable that they could not. It is only if the obligation to hold or retain control of trust property is itself one of "the trusts" that may be delegated under section 25 that it could be so used.[35] However, even if section 25 could be employed to vest trust property in a nominee, there are a number of significant drawbacks to using it this way that have already been indicated.[36]

THE SPECIAL POSITION OF CHARITABLE TRUSTS

The Official Custodian for Charities

7.12 There are certain special provisions which are applicable to charitable trusts. The Official Custodian for charities acts as a custodian trustee,[37] though his functions are being reduced. The only forms of property that he is now able to hold as nominee are—

(1) land; and

[30] A custodian trustee could not act as a custodian on say, the IFMA Terms. A custodian under those Terms has much wider powers than does a custodian trustee.

[31] As substituted by the Powers of Attorney Act 1971, s 9.

[32] See above, paras 3.35 and following.

[33] See above, para 3.35.

[34] See above, para 7.4.

[35] The history of the section, which we have explained above at para 3.35, heightens the doubt. It cannot have been visualised that an individual trustee would transfer the legal title to the trust property to his or her delegate under section 25. That could only be done by *all* of the trustees. It is conceivable that a *bailment* of trust property might be possible under section 25.

[36] See above, para 3.37.

[37] Charities Act 1993, s 2. The Official Custodian is liable for loss or misapplication of any property only if it happens through his wilful neglect or default or that of his agent: *ibid*, s 2(5).

(2) any other property vested in him by virtue of an order of the Charity Commissioners made for the protection of a charity.[38]

He was required to divest himself of all other forms of property by 1997 and can no longer undertake to hold investments for a charity as custodian trustee.[39] Where the custodian did divest himself of property that he held, the charity trustees could nominate a person to hold such property as nominee for the charity.[40] That person was required to be an individual resident in, or a corporation with its place of business in England and Wales.[41]

7.13 The power conferred on charity trustees to employee a nominee where the Official Custodian had divested himself of assets that he was holding was of course a very limited one. However, we understand that the Charity Commissioners are willing to sanction both the appointment and remuneration of nominees by charity trustees in other cases,[42] and in particular, in relation to investments. Usually this is given on the condition that the nominee is a corporation that has a place of business in England and Wales (and is therefore amenable to the jurisdiction of the High Court).[43] The concern that underlies this is that in some states trusts are either not recognised or, even if they are, trust property is not treated as being distinct from the assets of the nominee so as to be beyond the reach of creditors. However, where trustees wish to invest overseas, the Charity Commissioners will authorise the use of a foreign corporate nominee provided that the trustees make sure that—

(1) in acting as nominee, the corporation is either subject to—

(a) regulation and supervision by a regulatory body or agency of government in the country in which it carries on business; or

(b) regular independent review by auditors with qualifications prescribed either by law or by such regulatory body or agency; and

(2) the property of the trust fund is segregated from any other property which is held by the nominee, and either—

(a) the fund has an enforceable proprietary interest in the property which is held for or on behalf of the fund by the nominee; or

(b) all reasonably forseeable obligations of the nominee to the fund are guaranteed by a reputable insurance company or in some other way

[38] Charities Act 1992, s 29(2). For the Commissioners' powers to act for the protection of charities, see Charities Act 1993, s 18(1).

[39] Charities Act 1992, s 29(1).

[40] Charities Act 1992, s 29(5).

[41] *Ibid*. The residence requirement ensures that the nominee is subject to the jurisdiction of the High Court.

[42] Under their powers to authorise dealings with charity property: see Charities Act 1993, s 26; and (1994) 2 *Decisions of the Charity Commissioners*, 30, 32.

[43] Information kindly supplied by the Charity Commission. This limitation reflects the terms of Charities Act 1992, s 29(5).

approved by the Charity Commissioners.[44]

In this way, charity trustees are in practice able to employ nominees, albeit subject to restrictions. It does, however, require an application for authority from the Charity Commissioners.[45]

THE CASE FOR REFORM

7.14 In Part II of this Paper we set out some of the reasons why trustees might wish to vest trust assets in nominees,[46] namely—

(1) to provide an administration service in relation to investments;

(2) to facilitate dealings by a discretionary fund manager;

(3) as one method of using CREST;

(4) in relation to overseas investments which are traded using computerised clearing systems; and

(5) where registered land is held in trust, to obviate the need for regular changes to the register when trustees change.

We would not pretend that this list is in any sense exhaustive.

7.15 We also highlighted two particular drawbacks to the use of nominees. The first lay in the risks that it posed for the beneficial owner of the assets.[47] We explained how, in relation to the safeguarding and administering of investments within the United Kingdom, these risks had been ameliorated by the designation of such activities as investment business for the purposes of the Financial Services Act 1986.[48] The protections afforded by that Act now apply to nominees offering such services. The second drawback lay in the loss of shareholder rights where investments were vested in nominees.[49] Although this problem remains so far unresolved, we noted that the Department of Trade and Industry and HM Treasury had recently consulted upon it in relation to nominees who held securities on a non-discretionary basis, with a view to legislating if the responses justified it.[50] We concluded that these two developments did go a considerable way to remove the objections that exist to the employment of

[44] We understand that the Charity Commission is considering the conditions on which it gives authority, to ensure that they comply with the requirements of European Community law.

[45] See above, para 3.41, where we note that the costs of such an application are likely to be in the region of £600 to £1,000.

[46] See above, paras 2.12, 2.13.

[47] See above, para 2.14.

[48] See above, para 2.15. As a result of the Investment Services Regulations 1995, 1995 SI No 3275, a European investment firm (as defined by reg 3 of those Regulations) may also carry on such business in the United Kingdom, provided that it meets the requirements of those Regulations.

[49] See above, para 2.16.

[50] *Ibid*.

nominees.[51]

7.16 There is evidence that trustees' inability to employ nominees has been widely recognised as a shortcoming for some time. First, in its Twenty-third Report, The Powers and Duties of Trustees, the Law Reform Committee recorded that the evidence it had received was "overwhelmingly in favour of relaxing the existing restrictions on the use of nominee services".[52] It recommended that trustees should be able to employ nominees, though it proposed restrictions on the bodies that could act as such,[53] a point that we address below. [54] Secondly, in one of the cases that we discussed in Part II of this Paper in which additional powers were sought by trustees on an application to the court under section 57 of the Trustee Act 1925,[55] the judge considered that the power to vest securities in a nominee was "obviously desirable".[56] Thirdly, The Law Society has been pressing for an extension of trustees' powers to enable them to employ nominees.[57] Fourthly, we are aware that there has for some time been considerable pressure on shareholders to transfer their shares into the hands of a nominee company as a response to the introduction of both CREST[58] and five-day rolling settlement.[59] The imposition of pressure in this way is not itself any reason for changing the law. However, such conduct may cause trustees to transfer shares to nominees in breach of trust without appreciating the implications of their actions.

7.17 We have therefore provisionally concluded that trustees should have a statutory default power to vest trust property in nominees and a power to employ custodians. These powers would replace the existing (but very limited) statutory power to employ a custodian[60] and the statutory duty to do so in one situation.[61] We explain the safeguards that we propose for beneficiaries and explain why we have rejected certain others that we also considered. Before we set out the powers that we propose, there is one highly technical point that we must briefly address.

7.18 If trustees are given power to vest trust property in a nominee, that nominee will hold the property on a bare trust for the trustees. As a bare trustee, the nominee must act in accordance with the directions given by the trustee except to the extent that the terms agreed between the parties otherwise provide. Subject to certain caveats that we

[51] See above, para 2.17.

[52] (1982) Cmnd 8733, para 4.22.

[53] *Ibid*, para 4.23.

[54] See para 7.29 .

[55] *Anker-Petersen v Anker-Petersen* (1991) 88/16 LSGaz 32; above, para 2.45.

[56] Transcript, p 13, *per* Judge Paul Baker, QC.

[57] See (1995) 92/20 LSGaz 33 - 34.

[58] For comment in the press, see, eg, Damian Reece, "Nominee threat to the private shareholder" *The Sunday Telegraph*, 12 February 1995, explaining that "[m]ore than 80,000 investors in [a named investment trust's] saving schemes have been told to hand over the legal ownership of their shares to a nominee company and to invest by direct debit in future. They have until Friday to comply... or lose the benefits of saving scheme membership". The reason given was the introduction of CREST.

[59] See, eg, Margaret Stone, "Are shareholders losing their grip on companies?", *Daily Mail*, 8 February 1995.

[60] Trustee Act 1925, s 21; above, para 7.6.

[61] Trustee Act 1925, s 7; above, para 7.7.

raise below, the trustees will in turn hold either some subsidiary equitable interest or their rights of enforcement against the nominee on a sub-trust for the beneficiaries. Although sub-trusts are well recognised in the United States of America,[62] the manner in which they operate in this country has never been authoritatively settled, though it has been long been accepted that an equitable interest under a trust can itself be held upon trust.[63] There are some English cases which suggest that where A holds property on trust for B and B declares him or herself to be a trustee for C, A holds directly on trust for C, and B drops out.[64] Both the circumstances in which this occurs and indeed whether it occurs at all, are controversial.[65] Furthermore, the nature of the interest which B holds on trust is uncertain. One view is that B has the equitable interest and that C has "a subsidiary equitable interest".[66] Another possible analysis would be to emphasise that trusts are part of the law of obligations as much as they are part of the law of property. As B is a trustee and is not therefore intended to have any beneficial interest in the trust property, it might be better to regard him or her as holding on trust for C the rights which he or she has against A, the head trustee.[67] Whatever may eventually prove to be the correct analysis, our concerns are—

(1) to avoid any possibility that the nominee may hold the property directly on trust for the beneficiaries, the trustees having "dropped out of the picture"; and

(2) to define precisely what the position of the trustees is in such a situation.

We have provisionally concluded that it would be appropriate to clarify the position in any legislation to avoid any possible doubt.

PROPOSALS FOR REFORM

Powers to employ nominees and custodians

7.19 **We provisionally recommend that—**

[62] See the discussion in W F Fratcher, *Scott on Trusts* (4th ed 1987) § 83.

[63] See *Gilbert v Overton* (1864) 2 H & M 110, 116; 71 ER 402, 405.

[64] See, eg, *Grainge v Wilberforce* (1889) 5 TLR 436, 437; *Grey v IRC* [1958] Ch 375, 382.

[65] For a review of the issues, see Brian Green, "Grey, Oughtred and Vandervell - A Contextual Reappraisal" (1984) 47 MLR 385, 395 - 399. The Law Commission is considering this question further as part of its work on the creation of trusts and dispositions of equitable interests.

[66] See P V Baker, (1958) 74 LQR 180, 182 (an untitled casenote on *Grey v IRC* [1958] Ch 375).

[67] There are a number of situations where a person holds property in a fiduciary capacity but where there is no split in the legal and equitable ownership of the property. The obvious case is that of the person entitled under the unadministered estate of a deceased person: *Commissioner of Stamp Duties (Queensland) v Livingston* [1965] AC 694; *Re Leigh's Will Trusts* [1970] Ch 277; *Marshall v Kerr* [1995] 1 AC 148. In such a case "each such legatee or person so entitled is entitled to a chose in action, viz a right to require the deceased's estate to be duly administered, whereby he can protect those rights to which he hopes to become entitled in possession in the due course of the administration of the deceased's estate": *Re Leigh's Will Trusts*, above, at p 281, *per* Buckley J. The rights of an object under a discretionary trust are similar: "he has a right to be considered as a potential recipient of benefit by the trustees and a right to have his interest protected by a court of equity": *Gartside v IRC* [1968] AC 553, 617, *per* Lord Wilberforce. Such a right "is more than a mere spes": *ibid*, at p 618. Where trustees vest trust property in a nominee then, even if they do not have some *scintilla* of equitable title to the property, they certainly have rights which they can enforce against the nominee as bare trustee. Such rights may in part be contractual, but they may also constitute an equitable chose in action to compel the nominee to act at the direction of the trustees. Such an equitable chose in action is of course a transmissible proprietary right: *Re Leigh's Will Trusts*, above; *Marshall v Kerr*, above.

(1) trustees should have a power to vest trust assets in the name of a nominee, provided that such person acts as a nominee in the course of its business, and that for these purposes, "trust assets" should be widely defined to include both choses in action and any legal or equitable property rights that the trust might have; and

(2) the effect of employing a nominee under this power should be stated in statutory form so as to make it clear that—

(a) the nominee would hold the property to the order of the trustees in accordance with the terms agreed between the parties; and

(b) the trustees would hold the benefit of their rights against the nominee on the applicable trusts.

7.20 **We provisionally recommend that trustees should have a power to deposit trust documents (whether of title or otherwise) or trust property[68] with a custodian for safe keeping, provided that such person is a custodian in the course of its business. This power would be without prejudice to the existing right of trustees to leave trust documents in the custody of one of the trustees. We ask whether readers agree with the proposed powers.**

7.21 In view of the risks that may exist where nominees and custodians are employed,[69] we have formed the provisional view that trustees who take advantage of the new powers should review their arrangements at reasonable intervals. This is consistent with the provisional approach which we have put forward in relation to agents, namely that trustees should not only exercise an appropriate standard of care in relation to the appointment of an agent, but also in relation to supervising him or her thereafter.[70] We are aware that this may be regarded as an unnecessarily bureaucratic requirement and that it might place an unwarranted burden on trustees if they were required to undertake such reviews in the absence of some circumstance which makes it prudent to do so. We would therefore particularly welcome comments on this proposal.

7.22 **As a safeguard to beneficiaries, we provisionally recommend that trustees who employ a nominee or custodian under the powers proposed in paragraphs 7.19 and 7.20 should be under an obligation to review the employment at reasonable intervals. We ask whether readers agree, or whether they think that such an obligation is either unnecessary or should be more restricted in some way.**

7.23 Some of the issues that we have discussed in relation to the employment of agents apply equally to the engagement of nominees and custodians. Indeed, when a nominee or custodian is employed by trustees, that person may also be engaged as an agent, as in the common cases where a nominee settles transactions or collects income from investments. To achieve consistency, we consider that trustees should have similar powers in relation to the terms of employment and remuneration of nominees and

[68] Such as works of art, heirlooms, jewellery etc.

[69] See above, para 7.15.

[70] See above, para 6.45.

custodians as we have provisionally proposed as regards agents.[71] We are aware that those who provide nominee and custody services often contract on the basis that they may sub-delegate these functions.[72] They may also seek to restrict their liability.[73] We do not consider that it is necessary to give trustees authority to sanction possible conflicts of duty or interest by the nominee or custodian, because such situations are unlikely to arise.[74]

7.24 **We provisionally recommend that trustees should have power—**

(1) to pay custodians and nominees their reasonable fees; and

(2) where it is reasonably necessary to do so—

(a) to authorise the nominee or custodian to sub-delegate any of its functions to a sub-nominee or sub-custodian; and

(b) to employ nominees and custodians on terms which limit their liability.

We ask whether readers agree.

7.25 At present, where trustees deposit documents with a custodian under section 21 of the Trustee Act 1925, or bearer securities with a bank under section 7 of that Act,[75] the costs must be paid out of the *income* of the trust. As we have explained, any other expenditure incurred by the trustees is, by contrast, charged to *capital*.[76] Under our proposed powers, many nominees and custodians will also be employed as agents by trustees. There are obvious difficulties for trustees in allocating the costs of employing such persons if the present rule that custodians should be paid out of income is carried forward to the proposed new powers. **We provisionally recommend that trustees should have a discretion to allocate the costs of employing a nominee or custodian between income and capital. We ask whether readers agree.**

7.26 As we have already indicated, trustees have power to allow one of their number to have custody of the documents relating to the trust and, presumably, of any trust chattels.[77] Indeed, it would be inconvenient if the rule was otherwise. It is very much less obvious to us that it is desirable for one of the trustees to be able to act as a nominee, so that the title to the trust property is vested in him or her alone. There are obvious dangers to the beneficiaries in allowing such a delegation, and it does not seem to us to be appropriate to confer on trustees a default power to vest trust property in just one or some of them. **We provisionally recommend that there should be no power for trustees to vest trust property in one or some of their number as nominees in**

[71] See above, paras 6.34, 6.37, and 6.42, and the discussion at paras 6.35 and following.

[72] See, eg, IFMA Terms, cl C1(b).

[73] See *ibid*, cl C5.

[74] If the nominee or custodian is also acting as agent, such conflicts may arise, but we have already addressed this issue: see above, paras 6.38, 6.39.

[75] See above paras 7.6, 7.7.

[76] See above, para 6.30.

[77] See above, para 7.2(3).

the absence of express authorisation in the instrument creating the trust. Do readers agree?

7.27 Finally, we consider that the rule that trustees cannot make an investment jointly with one or more other persons[78] should be abrogated. It rests on the same principle of control that presently precludes the employment of nominees. **We provisionally recommend that trustees should have power to acquire and to hold property for the trust jointly or in common with other persons.**

Protection for beneficiaries

Possible options

7.28 We have outlined above the risks that may arise from the use of custody services.[79] It is obviously important that there should be appropriate protection for beneficiaries. We have considered three possible safeguards for them, namely—

(1) by restricting the range of persons who may act as nominees and custodians;

(2) by giving trustees a power to insure against the loss of or damage to either the trust property or indicia of title to such property, when vested in a nominee or deposited with a custodian, whether that loss or damage occurs by accident, or by the fraud or negligence of the nominee or custodian or its employees or agents; and

(3) by laying down appropriate duties of care which trustees must exercise in relation to the selection, appointment and supervision of nominees and custodians.

We have provisionally rejected the first two of them, but consider that the third should be adopted.

[78] See above, para 7.2(1).

[79] See para 7.15.

Restricting the persons that can act as nominees and custodians

TRUSTS OTHER THAN CHARITABLE TRUSTS

7.29 When the Law Reform Committee proposed that trustees should be given power to employ nominees,[80] they tempered their recommendation with the rider that only banks, trust corporations and stockbroking companies which were members of the Stock Exchange should be able to act as nominees in the absence of an express power in the trust instrument.[81] After careful consideration, we have concluded that there should be no restriction on the bodies which trustees might employ as nominees or custodians.

7.30 First, it would be difficult to define what those restrictions might be. As we have explained, the custody of investments[82] is now regulated by the Financial Services Act 1986.[83] It would therefore be possible to restrict the right of trustees to employ only those persons whose business was so regulated.[84] But not all cases where property is either vested in a nominee or deposited with a custodian are regulated by that Act. For example, neither a person who acts as a nominee solely in respect of land holdings nor a custodian who offers merely a safekeeping service is conducting an investment business under the Financial Services Act 1986.[85] Nor will that Act apply where the assets are outside the United Kingdom.[86] In any event, although regulation under that Act does undoubtedly offer significant safeguards for investors, the last-resort compensation scheme available to private customers offers only limited protection if the nominee becomes insolvent.[87]

7.31 Secondly, there is a danger that any such restriction might create the false impression that compliance with the specified criteria amounted to a "safe haven" for trustees and was a substitute for the exercise of proper prudence in selecting and controlling a nominee or custodian.

7.32 **Our provisional view is that, subject to the special position of charities, there should be no restrictions on the bodies that trustees might employ as nominees**

[80] Twenty-third Report, The Powers and Duties of Trustees (1982) Cmnd 8733, para 4.22; above para 7.16.

[81] *Ibid*, para 4.23.

[82] For these purposes, investments are defined by Financial Services Act 1986, Schedule 1, Part I.

[83] See above, paras 2.9, 2.15.

[84] Together with European investment firms which carried on safekeeping and administration in the United Kingdom: see Investment Services Regulations 1995, 1995 SI No 3275.

[85] In the former case this is because land is not an investment listed in Financial Services Act 1986, Schedule 1, Part I. In the latter case this is because it is only "safeguarding *and administering*" investments that is regulated under Financial Services Act 1986, Schedule 1, Part I, para 13A: see Custody: A Consultation Paper by HM Treasury (June 1996), para 15.

[86] Though there may no doubt be equivalent forms of protection in other states. That is of course the thinking that underlies the Investment Services Directive: Council Directive 93/22/EEC (OJ L141, 10.5.1993, p 27) that is implemented in this country by Investment Services Regulations 1995, 1995 SI No 3275.

[87] See above, para 2.11. We note that in cases of insolvency, in the absence of fraudulent misapplication by the nominee or custodian, the investor should not be at risk of losing his or her assets, because they were held by the nominee or custodian in a fiduciary capacity and would not therefore be available to creditors. However, even in these circumstances, there might be problems of tracing a particular investor's assets.

or custodians and we ask whether readers agree with us.

CHARITABLE TRUSTS

7.33 We have already explained that it is the practice of the Charity Commissioners to give charity trustees authority to vest trust property in nominees,[88] but that the authority is usually limited either to corporations that have a place of business in England and Wales so as to be amenable to the jurisdiction of the High Court, or where the nominee is overseas, subject to certain conditions.[89] If the power to employ nominees is made statutory, the Charity Commissioners will no longer have the ability to impose restrictions of this kind on the employment of nominees. To meet the concerns which have led the Charity Commissioners to impose conditions when granting charity trustees powers to employ nominees, it would be possible to devise statutory restrictions having a similar effect. We do not consider that it would be appropriate to formulate detailed conditions at this stage.[90] However, we would welcome comments on the principle of such restrictions. **We ask readers whether there should be statutory restrictions on the nominees which may be employed by charitable trusts to ensure a higher degree of protection for the trust fund.**

Power to insure against the defaults of the nominee or custodian

7.34 The second possible safeguard would be to give trustees power to insure against any loss to trust assets that might be suffered when they were vested in a nominee or deposited with a custodian.[91] The cost of that insurance would, of course, be borne by the trust. We have a number of objections to this. First, such insurance, although available, is expensive. Secondly, it is in practice very unusual for trustees to take out cover against this risk. As such, it is not an obvious candidate for inclusion in legislation as a default power. Thirdly, if such a power were conferred, trustees might feel that they would be in breach of trust if they failed to take out such insurance. This could lead to needless expenditure of trust money. Fourthly, to confer such a power might encourage trustees to think that such insurance was an acceptable substitute for the careful selection and supervision of the nominee or custodian.[92] We therefore provisionally reject this possible safeguard as well.

7.35 **Our provisional view is that trustees should not be given a default power to insure against loss caused by the acts, neglects and defaults of any nominee or custodian which they employed. Do readers agree?**

Duties of care

7.36 What does seem to us to be the right safeguard is to require appropriate standards of care by trustees in the selection and supervision of nominees and custodians. The issues are very similar to those which we have already discussed in Part VI in relation

[88] On an application under Charities Act 1993, s 26.

[89] See above, para 7.13.

[90] We would wish to discuss these in detail with the Charity Commissioners and others expert in the field of charity law. Any restrictions would of course comply with the requirements of European Community law.

[91] Trustees' powers to insure the trust property are explained in Part IX of this Paper.

[92] This point was made to us strongly by the Charity Commissioners.

to agents,[93] and we therefore put forward similar options for consideration. We would add that matters such as whether a body is regulated under the Financial Services Act 1986 or the extent (if any) of its insurance cover,[94] are precisely the sorts of issues that trustees can reasonably be expected to consider in selecting a nominee or custodian.

7.37 **Our provisional view is that there should be one standard of care expected of trustees in relation to the employment of nominees and custodians under the powers which we have proposed and that it should apply to each of the following matters—**

(1) the selection of any nominee or custodian;

(2) the terms on which that person is employed; and

(3) the supervision of that person once appointed.

We ask whether readers agree.

7.38 **Should the standard of conduct expected of trustees when appointing and controlling a nominee or custodian be that they should—**

(1) act in good faith;

(2) be vicariously liable for all the acts and defaults of their nominee or custodian;

(3) be required to satisfy a series of specified criteria, compliance with which would be a defence to any proceedings;

(4) be required to act with the care of the ordinary prudent person of business; or

(5) act with the care and diligence that may reasonably be expected having regard to the nature, composition and purposes of the particular trust, the skills which the trustees actually have, or if they are employed as professional trustees, those which they either ought to have or hold themselves out as having?

7.39 As we have made clear in relation to trustees' powers of delegation, our provisional view is that the choice lies between options (4) or (5). Option (1) would not set a sufficiently high standard. Option (2) would be too stringent. Our objections to option (3) are clear from what we have said in paragraphs 7.30 and 7.31 above.

7.40 In Part VI we also provisionally recommended that the standard of care applicable to the statutory power of delegation ought also to apply to any express power of delegation contained in the trust deed unless some other standard was expressly or

[93] See paras 6.44 and following.

[94] On such default insurance, see above, para 2.15. Trustees may have very good reasons for choosing a nominee or custodian which did *not* have such cover, as where they considered them to be the best person available for the trust's particular purposes.

impliedly specified in the trust instrument.[95] We consider that the same should be true in relation to any express power to appoint a nominee or a custodian. **We ask whether readers agree with our provisional view that the same standard of care that readers select in relation to the proposed statutory power to employ nominees and custodians should apply equally to any express power to employ such persons conferred by the instrument creating the trust unless some other standard is expressly or impliedly specified in that instrument.**

TO WHICH TRUSTS SHOULD THE NEW POWER APPLY?

7.41 As we indicated in Part I of this Paper, although it is now normal to include an express power to employee nominees when drafting a trust deed or will trust, this development is a comparatively recent one.[96] There are therefore many trusts in existence that do not contain such a power. Given that such a power is likely to be valuable to many trustees for the reasons that we have indicated above,[97] we consider that it should be applicable to existing trusts as well as those created after any legislation. This follows what we have already proposed in relation to powers of delegation.[98] **We therefore provisionally recommend that the proposed powers should apply to trusts whether created before or after any legislation was brought into force unless a contrary intention was expressed in the instrument creating the trust. Do readers agree?**

7.42 Subject to what we have said above about a possible restriction on the range of persons that should be able to act as nominees and custodians for charitable trusts,[99] we consider that the proposed powers to employ nominees and custodians should apply to all types of trust, including charitable trusts and pension trusts. There may be special considerations applicable to pension trusts of which we are unaware, and we shall be grateful for any comments on this point. **Subject to the provisional recommendation in paragraph 7.33 above, we propose that any new powers to employ nominees and custodians should apply to all types of trust, including charitable trusts and pension trusts. We ask whether readers agree with us.**

[95] See above, para 6.56.

[96] See above, para 1.8.

[97] See paras 7.14 - 7.16.

[98] See above, paras 6.58 and 6.60. We have not made any specific recommendation that trustees which have had their powers extended by order of the court or the Charity Commissioners should have the additional powers (as we have in relation to powers of delegation). This is because we doubt that our proposed powers are likely to be any more extensive than those given by the court or the Commissioners. However, we shall be interested to learn if this perception is wrong, because we are concerned to ensure that all trustees should have the powers proposed unless the settlor has excluded them.

[99] See para 7.33.

PART VIII
TRUSTEES' POWERS TO PURCHASE LAND

INTRODUCTION

8.1 In this Part we make proposals to extend trustees' powers in relation to the purchase of land. We have been prompted to make them by a discrepancy that exists between the powers of trustees of personal property and those of trustees where land is held in trust. The present law can be summarised as follows. In the absence of express authority in the trust instrument, trustees of personal property do not have power either to invest in the purchase of land or to acquire land as a residence or otherwise for the use of any beneficiary. By contrast, where land is held in trust, whether under a trust of land or a settlement under the Settled Land Act 1925, the trustees have power to purchase more land not only by way of investment, but for any other reason. We explain the law more fully in the following paragraphs.

THE PRESENT LAW

Powers of trustees of personal property

8.2 Although mortgages of either freehold land or of leaseholds having at least sixty years to run are authorised as a trustee investment,[1] the purchase of freehold land is not, unless it is either specifically sanctioned by the trust instrument or the trust is a pension trust.[2] As we explained in Part II,[3] it had been intended both to make an Order under the Deregulation and Contracting Out Act 1994, to remove a number of restrictions on trustee investment,[4] and to extend trustees' powers of investment further by an Order under section 12 of the Trustee Investments Act 1961. As a result of the dissolution of Parliament prior to the General Election, there was insufficient time for either of these Orders to be made. HM Treasury had not in fact indicated how it intended to extend the list of authorised investments in the proposed section 12 Order. It is not therefore known whether it was intended to give trustees power to invest in land.[5]

8.3 Even where trustees are given an express power to invest in the purchase of land (as they commonly are), that power may be more limited than it might be expected to be. The authorities suggest that in the context of trustees' powers—

(1) the term "investment" is not a term of art;

(2) its precise meaning cannot be regarded as settled; and

[1] Trustee Investments Act 1961, Sched 1, Part II, para 13. As the law stands, such mortgages are narrower-range investments which require advice: *ibid*, s 6(2).

[2] Pension trustees have the same powers of investment as a beneficial owner in the absence of any restriction imposed by the pension scheme: Pensions Act 1995, s 34(1): see above, para 3.43.

[3] See above, paras 2.5 and following.

[4] See the draft Deregulation (Trustee Investments) Order.

[5] We note however that, in evidence to the Select Committee of the House of Lords on Delegated Powers and Deregulation, John Mowbray QC and Alexandra Mason, on behalf of the Chancery Bar Association, expressed the view that an Order under section 12 could properly confer on trustees the same powers to invest as are enjoyed by a private individual: see the Twenty First Report of the Select Committee of the House of Lords on Delegated Powers and Deregulation, (1996-97) HL Paper No 70, p 32. See above, para 2.6.

(3) it appears to be subject to a significant limitation.

8.4 The understanding of what constitutes an investment is of course conditioned by the fiduciary duty of trustees to maintain an even hand between life tenant and remainderman.[6] The orthodox view has therefore been to regard the obligation to make investments as a duty to obtain income while maintaining the value of the capital.[7] More recent statements have however taken a broader view. In particular, it is now regarded as appropriate for trustees to seek capital growth as well as income yield.[8]

8.5 A significant limitation on what constituted an "investment" emerged in *Re Power*.[9] In that case, Jenkins J held that a express power in a will trust to invest in any manner that the trustee thought fit as if he were sole beneficial owner, "including the purchase of freehold property in England or Wales", did not authorise the purchase of a house for the testator's widow to live in.[10] Such a purchase was "not necessarily an investment, for it is a purchase for some other purpose than the receipt of income."[11] This decision did of course rest on the narrower view of "investment" that was then current. Although it was criticised at the time,[12] it has never been expressly doubted. It has in fact since been held that property "acquired merely for use and enjoyment" was not an investment.[13] A formidable case can certainly be made against the decision in *Re Power*. In particular, there is distinguished authority in relation to land held on trust for sale[14] that a "beneficiary's possession or occupation is no more than a method of enjoying in specie the rents and profits pending sale in which he is entitled to share".[15] In other words, the beneficiary's occupation can be equated to the receipt of income, so that the purchase of land could be regarded as an "investment" even on the

6 For this obligation, see above, para 5.12.

7 See, eg, *Re Somerset* [1894] 1 Ch 231, 247, where Kekewich J stated, in relation to an investment by trustees in a mortgage, that it should be one which will "not only... yield the stipulated income, but will ultimately and whenever required, realise the full sum advanced". In *Re Wragg* [1919] 2 Ch 58, 64, P O Lawrence J considered that "the verb 'to invest'... may safely be said to include as one of its meanings 'to apply money in the purchase of some property from which interest or profit is expected and which property is purchased in order to be held for the sake of the income which it will yield'". That definition was not intended to be exhaustive and was merely inclusive: see R E Megarry (1947) 63 LQR 421, 422.

8 See *Cowan v Scargill* [1985] Ch 270, 287, where Megarry V-C held that the power of investment "must be exercised so as to yield the best return for the beneficiaries, judged in relation to the risks of the investments in question; and the prospects of the yield of income and capital appreciation both have to be considered in judging the return from the investment". Similarly, in *Harries v The Church Commissioners for England* [1992] 1 WLR 1241, 1246, Nicholls V-C considered that where property was held by trustees as an investment "prima facie the purposes of the trust will be best served by the trustees seeking to obtain therefrom the maximum return, whether by way of income or capital growth, which is consistent with commercial prudence". See too *Nestle v National Westminster Bank Plc* [1993] 1 WLR 1260, 1283.

9 [1947] Ch 572.

10 She was the life tenant.

11 [1947] Ch 572, 575.

12 See the note on the case by R E Megarry in (1947) 63 LQR 421.

13 *Re Peczenik's Settlement Trusts* [1964] 1 WLR 720, 723, *per* Buckley J. The case was concerned with the scope of an express power of investment.

14 Trusts for sale now take effect as trusts of land: see Trusts of Land and Appointment of Trustees Act 1996, s 1(2).

15 *City of London Building Society v Flegg* [1988] AC 54, 83, *per* Lord Oliver of Aylmerton.

narrower view of that term which requires that the asset must be income producing. However, in the circumstances, *Re Power* must be taken as still representing the present law, notwithstanding the criticisms that can be made of it.

Powers of trustees where land is held in trust

8.6 Where land is held upon trust, the position is quite different. After 1996, there are two main ways in which land may be so held.[16] First, land that was settled land[17] prior to 1997, remains so, unless and until it ceases to be so under the provisions of either the Settled Land Act 1925 or the Trusts of Land and Appointment of Trustees Act 1996.[18] No new settlements can be created however.[19] The legal estate will generally be vested in the tenant for life. He or she will hold it on the trusts of the settlement, and will have statutory powers of disposition in relation to it together with any additional powers conferred by the settlement.[20] Secondly, the property may be held on a trust of land. The legal estate is then vested in the trustees who have "in relation to the land subject to the trust all the powers of an absolute owner".[21]

Settled land

8.7 Under the Settled Land Act 1925, any capital money that arises[22] may be "invested or otherwise applied" by the trustees of the settlement for one or more purposes specified by the Act.[23] These include the "purchase of land in fee simple, or of leasehold land held for sixty years or more unexpired at the time of purchase".[24] It has long been settled that the words "invested or otherwise applied" are to be read disjunctively.[25] An "application" of capital money need not therefore be an "investment". It follows therefore that if part of the settled land is sold, another property may be purchased with the proceeds of sale for the occupation of the life tenant.

[16] Land that is subject to the provisions of the Universities and College Estates Act 1925, which affects certain universities and colleges, is subject to the distinct statutory régime laid down in that Act. It is unaffected by the provisions of the Trusts of Land and Appointment of Trustees Act 1996: see s 1 of that Act.

[17] On what constitutes 'settled land', see Settled Land Act 1925, ss 1, 2. This definition is adopted by the Trusts of Land and Appointment of Trustees Act 1996, s 23(2), referring to Law of Property Act 1925, s 205(1)(xxvi).

[18] See respectively Settled Land Act 1925, s 3; and Trusts of Land and Appointment of Trustees Act 1996, s 2.

[19] Trusts of Land and Appointment of Trustees Act 1996, s 2(1), but note the qualification in s 2(2).

[20] For the statutory powers, see Part II of the Settled Land Act 1925. Those powers may be extended but not restricted: *ibid*, s 106. Any capital monies arising from any such disposition must be paid to the trustees of the settlement, not to the life tenant: *ibid*, s 75(1). See too s 94.

[21] Trusts of Land and Appointment of Trustees Act 1996, s 6(1).

[22] As, for example, from a sale of part of the settled land. If *all* of the settled land is sold and there is neither any land nor heirlooms that are subject to the settlement (cf Settled Land Act 1925, s 67(1)), but only the proceeds of sale, the settlement terminates: Trusts of Land and Appointment of Trustees Act 1996, s 2(4).

[23] Section 73. The application will usually be at the direction of the tenant for life, in default of which it will be at the discretion of the trustees: *ibid*, s 75(2).

[24] *Ibid*, s 73(1)(xi).

[25] See *Re Duke of Marlborough's Settlement* (1886) 32 ChD 1, 5, 10; *Re Earl of Egmont's Settled Estates* [1906] 2 Ch 151, 157.

Land held on a trust of land

8.8 Where land is held on a trust of land, under the Trusts of Land and Appointment of Trustees Act 1996, the trustees have a statutory power to "purchase a legal estate in any land in England or Wales".[26] That power may be exercised "by way of investment, for occupation by any beneficiary, or for any other reason".[27] The power applies not only to trustees of land, but also to trustees of the proceeds of sale of land.[28] If, therefore either—

(1) trustees of land sell all the land which they hold; or

(2) a life tenant under a Settled Land Act settlement sells all the property[29] subject to the settlement, so that the settlement thereby ceases;[30]

the trustees may still invest the proceeds of sale in the purchase of land, and they thereupon become trustees of land, with all the powers conferred by the 1996 Act.[31]

8.9 This statutory power to purchase land was enacted in response to a recommendation from the Law Commission that "trustees should have a broad power to apply some or all of any proceeds of sale to the purchase of land, either as an investment or for occupation by the beneficiaries".[32] At the time of the Commission's Report, although trustees for sale had a power to purchase land, it had been restrictively interpreted.[33] In particular, as a result of the decision in *Re Power*,[34] it could not be exercised to provide a home for a beneficiary.

CRITICISMS OF THE PRESENT LAW

[26] Section 6(3).

[27] Section 6(4). An example of a purchase of land "for any other reason" might be where property was acquired for a beneficiary to use for business or professional purposes rather than for a residence.

[28] Section 17(1).

[29] Whether land or heirlooms.

[30] See Trusts of Land and Appointment of Trustees Act 1996, s 2(4).

[31] Section 17(1) of the 1996 Act was enacted in order to correct a point that arose in relation to land held upon trust for sale prior to 1997. Trustees *for sale* had the power to invest or apply capital money in the purchase of land: Law of Property Act 1925, s 28(1); Settled Land Act 1925, s 73(1)(xi); *Re Wellsted's Will Trusts* [1949] Ch 296. However, if they sold *all* the land (as opposed to merely part of it), they ceased to be trustees *for sale* and were merely trustees of personal property. They could not therefore purchase land: *Re Wakeman* [1945] Ch 177. This led to the absurdity that, if they retained even a "minute quantity" of land, they were still trustees for sale and could purchase land, but not if they sold it all: *ibid*, at p 181, *per* Uthwatt J.

[32] Transfer of Land: Trusts of Land (1989) Law Com No 181, para 10.8. The draft Bill attached to that Report differs significantly from the Trusts of Land and Appointment of Trustees Act 1996 which eventually enacted the Law Commission's recommendations. Clause 4 of that draft Bill would have given trustees power to purchase land "for any purpose they think fit". In practice, the wording of section 6(4) of the 1996 Act ("by way of investment, for occupation by any beneficiary, or for any other reason") may not differ in substance from what the Commission originally proposed. It seems probable that the fuller wording that was finally adopted was intended to assist trustees by making it explicit that they did actually have power to purchase a property for occupation.

[33] Transfer of Land: Trusts of Land, above, at para 10.7.

[34] [1947] Ch 572; above, para 8.5.

8.10 There are a number of criticisms that can be made of the present law. First, trustees's inability to purchase land has become an inconvenient restriction on their powers. It has been the frequent practice for some time to include an express power to purchase land for use by a beneficiary in a trust instrument.[35] This suggests that such a power is not only regarded as highly desirable, but is an appropriate one to include as a statutory default power. We note that, prior to its Report of 1982, The Powers and Duties of Trustees, the Law Reform Committee sought views on this issue on consultation. The evidence it received was "overwhelmingly in favour" of widening trustees' powers to enable them to purchase land both as an investment and to provide a house for one or more of the beneficiaries.[36] The Committee duly recommended that trustees' powers should be extended in that way.[37] Secondly, the correctness of the decision in *Re Power*[38] - that the purchase of land to provide a home for a beneficiary is not an "investment" - is, as a matter of law, open to doubt.[39] Thirdly, the present law can operate somewhat capriciously. If trustees of personalty have a power in the trust instrument[40] to invest in land, and do so, they then become trustees of land. Although they cannot use *that* land as a residence for a beneficiary, they may sell it and purchase *other* land with the proceeds which *can* be used for that purpose. Such artificiality does little credit to the law.[41]

PROPOSALS FOR REFORM

8.11 In the light of these criticisms, we consider that there is a very strong case for extending the powers enjoyed by trustees of land to all other trustees (except trustees of the settlement under the Settled Land Act 1925 who already have equivalent powers). **We therefore provisionally recommend that—**

(1) all trustees (other than trustees of land and trustees of the settlement under the Settled Land Act 1925) should have power to purchase a legal estate in land in England or Wales; and

(2) trustees should be able to exercise that power—

(a) by way of investment;

(b) for occupation by any beneficiary; or

[35] See the Law Reform Committee's 23rd Report, The Powers and Duties of Trustees (1982) Cmnd 8733, para 3.5. We note that a number of those who responded to the consultation paper, Investment Powers of Trustees: A Consultation Document by HM Treasury, May 1996, specifically sought the extension of trustees' investment powers to include the purchase of land for use by a beneficiary. These included the General Council of the Bar and The Law Society.

[36] The Powers and Duties of Trustees, above, paras 3.2, 3.5.

[37] *Ibid*, Part IX (Summary of Recommendations), para 6.

[38] [1947] Ch 572. It must be noted that it was a decision of Jenkins J, who was one of the most distinguished chancery lawyers of the time.

[39] See above, para 8.5.

[40] Or by statute in the case of pension trustees: see Pensions Act 1995, s 34(1); above, para 3.43.

[41] This point was fully appreciated by us at the time when the Trusts of Land and Appointment of Trustees Bill was before Parliament. The Commission considered whether the power conferred by what is now s 6(3) of the Act should be extended to all trustees. However, we decided not to pursue the point at that stage. Any such extension would have required an amendment not only to section 6 but to the long title of the Bill. This might have created difficulties, given the very tight timetable for the Bill's passage.

(c) for any other means.

Once land has been purchased, the trustees would of course be trustees of land and would have the powers and duties laid down in the Trusts of Land and Appointment of Trustees Act 1996.

8.12 It is in our view desirable to add a supplementary power. Trustees who wish to purchase land as a residence for a beneficiary may not be able to raise the money except by selling other property. Although trustees of *land* have in relation to the land all the powers of an absolute owner[42] and can therefore purchase land with the aid of a mortgage, other trustees have no equivalent power.[43] We consider that such a power should be given to all trustees. We note that the Law Reform Committee in its Report, The Powers and Duties of Trustees, made similar recommendation.[44] The Committee would, however, have limited the power to borrow to not more than two-thirds of the value of the house.[45] Although we appreciate the good sense of that restriction, we doubt that it is necessary. The Trusts of Land and Appointment of Trustees Act 1996 imposes no such restrictions on trustees of land, and we consider that it is best to leave the matter to be regulated by the trustees' common law obligations to act with reasonable prudence in the best interests of the trust.[46] **We therefore recommend that, when exercising the proposed power to purchase land, trustees should be able to do so with the aid of a mortgage.**

TO WHICH TRUSTS SHOULD THE NEW POWERS APPLY?

8.13 From what we have said above,[47] it appears that many trustees (and beneficiaries) of existing trusts would welcome the additional powers that we propose. **We therefore provisionally recommend that the proposed powers should apply to all trusts whether they were created before or after any legislation was brought into force, unless a contrary intention was expressed in the instrument creating the trust. Such powers should be in addition to any more limited powers to purchase land that have either been—**

(1) conferred by the instrument creating the trust; or

(2) previously granted by the court or the Charity Commissioners.

[42] Trusts of Land and Appointment of Trustees Act 1996, s 6(1).

[43] See *Re Suenson-Taylor's Settlement Trusts* [1974] 1 WLR 1280. Prior to the decision in *Abbey National Building Society v Cann* [1991] 1 AC 56, where land was purchased with the aid of a mortgage, there was considered to be a "*scintilla temporis*" between the acquisition of the legal estate and the execution of the mortgage: see *Church of England Building Society v Piskor* [1954] Ch 553. If that view had remained the law, trustees who wished to purchase land with the aid of a mortgage would have become trustees of land when they acquired the legal estate and because of the notional *scintilla* of time between that acquisition and the execution of the mortgage would have acquired the necessary powers to execute the mortgage. However, in *Abbey National Building Society v Cann*, the House of Lords overruled the *Piskor* case and held that the acquisition of the legal estate and the mortgage were "not only precisely simultaneous but indissolubly bound together": see p 92, *per* Lord Oliver of Aylmerton.

[44] (1982) Cmnd 8733, para 3.11.

[45] *Ibid*.

[46] See above, paras 2.1, 4.2.

[47] See para 8.10.

PART IX
TRUSTEES' POWERS TO INSURE THE TRUST PROPERTY

INTRODUCTION

9.1 In this Part we consider trustees' powers to insure the trust property. Our survey is prompted by two factors. The first is the uncertainty both as to the extent of trustees' *powers* to insure and as to whether they are ever under a *duty* to do so in particular circumstances. The second is the anomalous state of the present law under which the statutory powers to insure differ according to the type of property and the way in which it is held in trust. We begin by explaining what the present law is and, in the light of our criticisms of it, we make recommendations for its reform.

THE PRESENT LAW

The position at common law

9.2 In *Re Betty*[1] North J suggested that at common law trustees ought to insure the trust property "at the expense and for the benefit of the estate". Against that view, there were two old cases in which it was held that executors who failed to insure trust property were not guilty of "wilful default".[2] Both cases were characterised by their special facts. In the first of them,[3] executors continued to run the deceased's business after his death jointly with his former partner. The partnership premises were not insured and were destroyed by fire. Alderson B concluded that there was no wilful default by the executors because the surviving partner had not insured the property either. He thought that it would be a "strong thing" to hold the executors liable for wilful default for failing to do what the surviving partner had also not done.[4] In his view, "the executors are only bound to do what a reasonable man might do".[5] In judging that, the "omission of the surviving partner, who was also interested to insure, affords the best criterion".[6] In the other case,[7] the testator was required to insure the premises by a covenant in the lease under which he held them. The insurance lapsed two days before he died and was not renewed. The property was burnt down two months after the testator's death and three weeks before the executors had proved the will. At the time of the fire, the executors had not been bound to perform the covenant to insure and were not therefore liable.

9.3 Despite their special facts, these cases were subsequently taken by Eve J in *Re*

[1] [1899] 1 Ch 821, 829.

[2] *Bailey v Gould* (1840) 4 Y & C Ex 221; 160 ER 987 (see too the report at 9 LJEx Eq 43 which gives a clearer explanation of the decision in the case); *Fry v Fry* (1859) 28 LJCh 593 (a better report than 27 Beav 144; 54 ER 56). In this context "wilful default" meant no more than the commission of some breach of duty: see above, paras 4.15, 4.16; and *Fry v Fry*, at p 594.

[3] *Bailey v Gould*, above.

[4] (1840) 4 Y & C Ex at 225, 226; 160 ER at 988.

[5] (1840) 9 LJEx Eq 43, 44.

[6] *Ibid*. This does seem a very questionable conclusion.

[7] *Fry v Fry*, above.

McEacharn[8] as laying down a general rule that, even where there was a power to insure, "the court will not hold an executor or trustee liable on the footing of wilful default for losses occasioned by fire on premises left uninsured by him".[9] This was so, even though, as the judge acknowledged, "most persons having property subject to loss or damage by fire would agree in considering an insurance against fire to be a prudent and proper precaution to adopt".[10] The issue in that case was whether the trustees, who had a statutory power to insure the premises held in trust against fire, were under a *duty* to exercise that *particular* power. Under the statutory power,[11] the trustees might insure the property against loss or damage by fire up to three-quarters of its value, and might pay the premiums out of the *income* of that property (or any other subject to the same trusts) without obtaining the consent of any person entitled to all or part of such income. One of the trustees was the life tenant and she objected to the exercise of the power. It may be inferred that she did so because the insurance would be paid out of income and therefore at her expense. Because the court concluded that the statute conferred only a *power* and not a *duty* to insure, it would not compel its exercise: trustees' powers must be exercised unanimously.[12]

9.4 Eve J deliberately left open the question whether the trustees "ought to insure the premises *at the expense of the estate generally*".[13] This was because the only question on the summons was whether such insurance ought to be maintained *at the expense of the tenant for life*. His choice of words suggests that he was mindful of North J's remarks in *Re Betty*[14] - which were cited to Eve J - that trustees had an obligation to insure at common law, meeting the cost out of *capital* at the expense of the estate. The view that there was such a power (and perhaps even a duty in certain circumstances) to insure at common law quite apart from any statutory power seems to have been accepted by Sir Benjamin Cherry, the draftsman of the Trustee Act 1925.[15] It has also been expressly endorsed in both Ireland[16] and New South Wales.[17] These authorities have led us to conclude that there is indeed such a power to insure, and that there may sometimes be a duty to do so.

[8] (1911) 103 LT 900.

[9] *Ibid*, at 902.

[10] *Re McEacharn*, above, at 902.

[11] Trustee Act 1893, s 18. This was re-enacted as Trustee Act 1925, s 19. For the substantially amended version of that power that now applies, see below, para 9.7.

[12] *Re McEacharn*, above, at 902.

[13] *Ibid* (italics added).

[14] [1899] 1 Ch 821, 829; above, para 9.2.

[15] See the comments on Trustee Act 1925, s 19(1) in Sir Benjamin Cherry, D H Parry and J R P Maxwell, *Wolstenholme & Cherry's Conveyancing Statutes* (12th ed 1932) Vol 2, pp 1292, 1293.

[16] "I think the trustees are bound to take care that the premises are insured against fire, so as to preserve the property for their *cestuis que trust*... .": *Kingham v Kingham* [1897] 1 IR 170, 174, *per* Chatterton V-C. This suggests a *duty* to insure.

[17] "While a trustee is not bound to insure the trust property, he should do so in the interests of the beneficiaries": *Davjoyda Estates Pty Ltd v National Insurance Company of New Zealand Ltd* [1965] NSWR 1257, 1266, *per* Brereton J, citing *Re Betty*, above.This suggests a *power* to insure.

Statutory powers

9.5 The statutory power to insure trust property dates back to 1888.[18] Prior to 1997 it was a power "to insure against loss or damage by fire any building or other insurable property".[19] However as a result of the Trusts of Land and Appointment of Trustees Act 1996,[20] there is now a distinction between the statutory powers of trustees of land and trustees of personal property. As we shall explain, trustees of the settlement of settled land have no *statutory* powers to insure.[21]

9.6 First, under the Trusts of Land and Appointment of Trustees Act 1996, trustees of land[22] have in relation to the land subject to the trust "all the powers of an absolute owner".[23] Those powers are however given "for the purpose of exercising their functions as trustees",[24] and we take this to mean that they must be exercised in accordance with trustees' fundamental obligations to act in the best interests of the trust and to take reasonable care of the trust property. Subject to that qualification, trustees of land have a power to insure the trust property whenever a beneficial owner of land might do so.

9.7 Secondly, the statutory powers of trustees of personal property are laid down in section 19 of the Trustee Act 1925, as amended by the Trusts of Land and Appointment of Trustees Act 1996,[25] and are as follows—

> (1) A trustee may insure any personal property against loss or damage to any amount, including the amount of any insurance already on foot,[26] not exceeding three fourth parts of the full value of the property, and pay the premiums for such insurance out of the income thereof or out of any income of any other property subject to the same trusts without obtaining the consent of any person who may be entitled wholly or partly to such income.
>
> (2) This section does not apply to any personal property which a trustee is bound forthwith to convey absolutely to any beneficiary upon being requested to do so.

There are three observations about this power that are relevant for present purposes. First, where it applies, the trustees may charge the cost of premiums to income without

[18] Trustee Act 1888, s 7.

[19] Trustee Act 1925, s 19(1), as originally enacted.

[20] Which came into force on 1 January 1997.

[21] See below, para 9.8.

[22] That is, trustees of "property which consists of or includes land" other than settled land or land subject to the Universities and College Estates Act 1925: Trusts of Land and Appointment of Trustees Act 1996, s 1.

[23] Section 6(1).

[24] *Ibid*.

[25] See ss 25(1), (2); Sched 3, para 3; Sched 4.

[26] The wording of the provision is hardly felicitous. "The words 'any amount, including etc, not exceeding, etc' apparently mean 'any amount not exceeding, together with the amount of any insurance already on foot, three-fourths, etc'": Sir Benjamin Cherry, D H Parry and J R P Maxwell, *Wolstenholme & Cherry's Conveyancing Statutes* (12th ed 1932) Vol 2, p 1292.

the need to obtain the consent of those entitled to that income. It therefore differs from the common law power to insure under which the premiums are charged to capital.[27] Secondly, although the power is in its present form limited to trustees of personal property where before 1997 it applied to all trustees, it is wider in scope because it empowers the trustees to insure "against loss or damage" and not merely to "loss or damage by fire". Thirdly, the power remains subject to two significant restrictions. The first is that trustees can only insure up to three quarters of the value of property, and we are unable to understand the reason for this. The second is that it does not apply where the trustees hold personal property on a bare trust. The concern underlying this seems to be that a beneficiary under the bare trust might not wish the trustees to insure the property. Although such a beneficiary can direct the trustees to convey the property at his or her direction, he or she cannot direct them as to the exercise of their powers.[28] However, there are better ways of overcoming this difficulty than by the complete exclusion of the statutory power to insure, and we make suggestions for meeting this point below.[29]

9.8 Thirdly, trustees of the settlement under the Settled Land Act 1925 have no statutory power to insure, although they did so prior to 1997.[30] This appears to have come about through an oversight in preparing the consequential amendments for the Trusts of Land and Appointment of Trustees Act 1996. The consequences of this omission are, however, hardly grievous. As we explain below,[31] trustees are at present well advised to insure to the full extent of the value of the trust property in question under their common law powers and to charge the costs to capital, rather than relying on the more limited statutory power and charging the premiums to income.

CRITICISMS OF THE PRESENT LAW

Specific criticisms

Uncertainty

9.9 One obvious reason for reforming the law is its uncertainty. It is not easy to advise trustees as to what their obligations as to insurance actually are under the present law. Although there are statutory powers to insure, they are not comprehensive. The authorities appear to establish the existence of an implied power at common law to insure, and there are suggestions in some cases that this is a positive duty. But trustees are at risk if they purport to exercise powers that they do not have or fail to exercise powers that they did not appreciate that they had been given. We consider that they are entitled to know exactly what their position is.

[27] See above, para 9.4.

[28] See *Re Brockbank* [1948] Ch 206.

[29] Paras 9.22, 9.23. Because of the unsatisfactory nature of these two restrictions, we considered the possibility of their repeal during the passage of the Trusts of Land and Appointment of Trustees Bill. However, we decided against seeking any such change at this stage for technical reasons that we have already explained in relation to another matter: see above, para 8.10. As we were working on the present Paper at that time, we considered it would be far better to deal with the point comprehensively.

[30] It is clear that Trustee Act 1925, s 19, as originally enacted, did apply to such trustees. Cf Trustee Act 1925, s 20, which deals with the application of insurance money received by trustees and explicitly applies to settled land.

[31] Para 9.11.

Conflict with trustees' duties to the trust

9.10 We have explained that it is the duty of trustees—

(1) "to exercise their powers in the best interests of the present and future beneficiaries of the trust";[32] and

(2) "to conduct the business of the trust with the same care as an ordinary prudent man of business would extend towards his own affairs".[33]

It is not easy to reconcile these fundamental principles with the authorities, considered above, which suggest that trustees are under no duty to insure.[34] This apparent contradiction has not gone unremarked,[35] and there must a real doubt whether a court would still adhere to the view expressed in *Re McEacharn*[36] that trustees are under no obligation to insure even in circumstances where a reasonable prudent person would do so.[37] If this old view does still hold good, it leaves beneficiaries without proper protection.[38]

Unsatisfactory nature of the statutory powers to insure and their application

9.11 The statutory power to insure given to trustees of personal property by section 19 of the Trustee Act 1925 is unsatisfactory, even in the wider form into which it was cast by the Trusts of Land and Appointment of Trustees Act 1996. Leaving aside the unhappy drafting of the section,[39] it suffers from two major defects—

(1) it only empowers trustees to insure up to three-quarters of the value of the property and not up to market value or full replacement value; and

(2) it has no application to bare trustees.

The first of these limitations again conflicts with a trustees' duty to manage the trust property with reasonable care. Indeed it has been suggested that "if an ordinary prudent person would insure up to full market value or full replacement value, it may be wise for trustees to do the same".[40] We have already commented on the second of

[32] *Cowan v Scargill* [1985] Ch 270, 286, *per* Megarry V-C; above, para 2.1.

[33] *Bartlett v Barclays Bank Trust Co Ltd (No 1)* [1980] Ch 515, 531, *per* Brightman J; above, para 6.52.

[34] See paras 9.2 - 9.4.

[35] See the Law Reform Committee's 23rd Report, The Powers and Duties of Trustees (1982) Cmnd 8733, para 4.29; Halsbury's Laws of England (4th ed reissue 1995) vol 48, para 891 n 1.

[36] (1911) 103 LT 900, 902; above, para 9.3.

[37] "No prudent trustee would fail nowadays to see that the trust premises are fully insured... it is arguable that trustees ought to be under a duty to insure against all those risks against which an ordinary modern prudent man of business would insure...": David J Hayton, *Underhill and Hayton: Law of Trusts and Trustees* (15th ed 1995) p 556, n 12. See too *Kingham v Kingham* [1897] 1 IR 170, 174; above, para 9.4.

[38] See Ann and Phillip Kenny, "The Underinsured Beneficiary" (1982) 79 LSGaz 755.

[39] See above, para 9.7.

[40] Halsbury's Laws of England (4th ed reissue 1995) vol 48, para 891 n 4.

these defects.[41]

9.12 More generally, we consider that it is unsatisfactory that—

(1) trustees of personal property and trustees of land should have different statutory powers of insurance; and

(2) trustees of the settlement of settled land should have no statutory powers to insure but must rely on their common law powers.

The approach in other jurisdictions

9.13 A number of the problems that we have identified above have been specifically addressed in other jurisdictions which have similar trustee legislation to our own. In Northern Ireland, for example, section 19 of the Trustee Act (Northern Ireland) Act 1958[42] provides—

> A trustee may insure against loss or damage by fire, explosion, impact, lightning, thunderbolt, storm, tempest, flooding, subsidence or landslip any building or other insurable property to any amount, including the amount of any insurance already on foot, not exceeding the full value of the building or property, and pay the premiums for such insurance out of the income thereof or out of the income of any other property subject to the same trusts without obtaining the consent of any person who may be entitled wholly or partly to such income.

Although the range of insurable risks is limited - it does not include theft for example - there are no restrictions on the extent to which the property may be insured, nor does it exclude property held upon a bare trust.

9.14 A number of Australian states have legislation in similar form.[43] There are variations between the states, but the power contained in section 41 of the Trustee Act 1925 of New South Wales[44] may be taken as typical—

> (1) A trustee may insure against loss or damage, whether by fire or otherwise, any insurable property, and against any risk or liability against which it would be prudent for a person to insure if he were acting for himself.
>
> (2) The insurance may be for any amount, provided that, together with the amount of any insurance already on foot, the total does not exceed the insurable value or liability.

The proposals of the Law Reform Committee

[41] See above, para 9.7.

[42] See Robert D Carswell, *Trustee Acts (Northern Ireland)* (1964) pp 45 - 46.

[43] Tasmania is alone in adhering to the form adopted in the English Trustee Act 1925, s 19, as originally enacted.

[44] We do not quote all of the subsections of this provision, but only those that are directly relevant.

9.15 The Law Reform Committee addressed trustees' powers to insure trust property in its Twenty-third Report, The Powers and Duties of Trustees.[45] Its comments were confined to trustees' statutory powers and it deliberately did not consider whether trustees had an implied power at common law to insure[46] which, as we have indicated, we understand to be the case.[47] The Committee's criticisms of the law were however very similar to our own. In particular they commented that "it is difficult to see how, in some circumstances, failure to insure would be consistent with [trustees'] general duty to take care of the trust property".[48] They recommended that all trustees should—

(1) "be placed under a duty to insure against any risk in all the circumstances in which an ordinary prudent man of business would so insure, but that this should not be imposed on existing trusts";

(2) "have the power to insure the trust property up to its full replacement value in all cases in which it would be sensible to do that, and in other cases up to its market value"; and

(3) "be empowered to pay insurance premiums out of capital as well as income but should make the payments in such a way as to maintain the balance between the interests of the life tenant and the interests of the remainderman".[49]

The Committee also recommended that "where the beneficial owner is the sole person interested in the preservation or maintenance of the trust property, he should be entitled to tell the trustee to cease to insure further and to surrender any existing policies".[50] As we indicate below, we agree with most but not all of what the Committee recommended.

PROPOSALS FOR REFORM

The issues

9.16 Given the uncertain and unsatisfactory state of the present law, we consider that there is an overwhelming case for providing a clear statutory power to insure that adequately protects the interests of the beneficiaries (or other objects of trust). There are five issues that require consideration. These are—

(1) what default powers of insurance should trustees have?

(2) in what circumstances, if any, should they be under a duty to exercise that power?

(3) should special provision be made where land is held either upon a bare trust or for beneficiaries who are all of full age and capacity and, taken together, are absolutely entitled to the trust property?

[45] (1982) Cmnd 8733, paras 4.29 - 4.37.

[46] See below, para 9.27.

[47] See above, para 9.4.

[48] The Powers and Duties of Trustees, above, para 4.29.

[49] *Ibid*, Part IX, paras 29 - 31.

[50] *Ibid*, para 4.35.

(4) should premiums be payable out of income or capital?

(5) to which trusts should the powers apply?

The power to insure

9.17 We consider that trustees should have the same powers to insure as a beneficial owner. This is already the position in relation to land held on a trust of land, and a power in such wide terms would obviate the need for any express powers of insurance in trust instruments in future (though settlors would of course be free to modify, exclude or restrict it). It would also make unnecessary any detailed provision about whether trustees should insure the property for its market value or its replacement value. They would have power to do either and could tailor the decision to the circumstances. The only objection that we can see to so broad a power is that trustees might insure in cases where it is unnecessary. However, this can be avoided by limiting the power in the same way as it is in relation to trusts of land. It would be given "for the purpose of exercising their functions as trustees".[51] This carries with it the obligations to act in the best interests of the trust and to take reasonable care of the trust property.[52] Trustees would therefore be expected to strike a balance between wasting trust money by insuring unnecessarily and placing the trust property at risk by failing to insure it when common prudence demanded it.[53] The power we propose would be wider than that which applies in, say, New South Wales,[54] because it would enable trustees to insure in any situation in which a reasonable person *might* insure, and not just in those cases where it was imprudent not to insure. We consider that this is fairer to trustees because it gives them more latitude in deciding what they think is best for the trust.

9.18 **We provisionally recommend that, for the purpose of exercising their functions as trustees, all trustees should have the same power to insure the trust property as they would if they were the absolute owners of it. We ask whether readers agree, or whether they consider that the power should be more limited or that the trustees' obligations should be more fully spelt out.**

A duty to insure?

9.19 We consider that there are circumstances in which trustees should not merely have a power to insure, but should be under a duty to do so. The point is significant for at least two reasons. First, a court will not normally order trustees to exercise a power if they are not unanimous as to its exercise. It will however direct the trustees to insure if they are under a duty to do so. Secondly, while a failure to exercise a power will not normally amount to a breach of trust, trustees who do not perform a duty will always commit a breach of trust. The statutory power to insure that we have proposed in the previous paragraph should be elevated to the status of a duty where it would be imprudent not to insure the trust property. The duty would not be discharged merely by taking out *some* insurance. The cover would have to be appropriate to the particular

[51] Trusts of Land and Appointment of Trustees Act 1996, s 6(1); above, para 9.6.

[52] See above, para 9.6.

[53] See below, para 9.20.

[54] See above, para 9.14, 9.15.

circumstances.[55]

9.20 It may be helpful to explain what the nature of trustees' obligations would be if they had both a power to insure and duty to exercise that power in certain circumstances. There would be situations where—

(1) it was wasteful for trustees to insure the trust property and where to do so would be a breach of trust, as where the trust property was a leasehold building and the landlord was required by the lease to insure the premises against fire and to apply the proceeds in their repair or reinstatement;

(2) trustees might insure, because a prudent person might reasonably do so, even though a failure to do so would not be imprudent, as where trustees insured trust property against a wider range of risks than was absolutely necessary; and

(3) a reasonable prudent person would have insured the premises so that trustees would be in breach of trust if they failed to do so, as where they failed to insure against fire or theft valuable paintings that were held on trust.

We would emphasise that it is not intended to impose an obligation on trustees to insure against all risks and in all circumstances. The test we propose is one of reasonableness which necessarily takes into account whether insurance is the most cost effective way of protecting the property. If a reasonable prudent person would not insure because the cost was prohibitive,[56] then the duty to insure would not apply, and the trustees would, no doubt, take other steps to ensure the safe-keeping of the property.

9.21 **We recommend that trustees should be under a duty to insure trust property—**

(1) in circumstances when;

(2) against such risks as; and

(3) for such amount as;

a reasonable prudent person would have insured the property. We ask whether readers agree.

[55] We do not think it necessary in this context to spell out with greater particularity this standard of conduct expected of trustees as we have proposed in relation to the selection and control of agents, nominees and custodians. The issue here is not whether the trustees have acted according to a particular standard, but whether they have identified the circumstances in which a reasonable prudent person would have insured the premises.

[56] As in the case of a major work of art that was in practice irreplaceable.

Bare trusts

9.22 We agree with the view of the Law Reform Committee that "[a]s a general rule the mere fact that a trustee is holding property of any description on a bare trust should not in any way alter or exclude the statutory powers of insurance".[57] However, where there is either a bare trust or all the beneficiaries are of full age and capacity and, taken together, are absolutely entitled to the trust property, we consider that the beneficiaries should be at liberty to direct the trustees *not* to insure the trust property if that was their unanimous wish. This power to direct the trustees would be strictly confined to those situations where the beneficiaries could put an end to the trust under the rule in *Saunders v Vautier*.[58]

9.23 **We provisionally recommend that—**

(1) both the statutory power and the statutory duty to insure which we propose should apply where property is held either—

(a) on a bare trust for a beneficiary absolutely; or

(b) for beneficiaries who are of full age and capacity and, taken together, are absolutely entitled to the trust property; but

(2) in those circumstances, if the beneficiaries all agree, they should be able to direct the trustees not to insure the property.

Do readers agree?

9.24 A related issue arises if our recommendations in Part VII are accepted and trustees are given power to vest trust property in nominees.[59] The nominees would themselves be trustees and would therefore have the powers and duties to insure that we have proposed above. We consider however that the trustees should be able to direct the nominees not to insure the property. This would cover the case where, for example, the trustees had a policy of insurance covering all the trust property and did not wish to see expenses unnecessarily incurred by the nominee on further insurance.

9.25 **We provisionally recommend that where trust property has been vested by trustees in nominees, the trustees shall have power to direct the nominees that they shall not insure the property. We ask whether readers agree with us.**

Should premiums be paid out of income or capital?

9.26 As we have explained, under the present statutory power to insure personal property held on trust, the trustees may meet the costs of premiums out of income.[60] If they insure under the common law power, they may charge the cost of the premiums to

[57] See its 23rd Report, The Powers and Duties of Trustees (1982) Cmnd 8733, para 4.35.

[58] (1841) 4 Beav 115; 49 ER 282. In essence, that rule states that where all the beneficiaries are (a) of full age and capacity; (b) are between them absolutely entitled to the trust property; and (c) unanimously agree; they may direct the trustees to convey or transfer the trust property to them or in accordance with their wishes, in whatever manner they think fit.

[59] See above, paras 7.19 and following.

[60] Trustee Act 1925, s 19 (as amended); above, para 9.7.

capital.[61] As regards the former, there are obvious difficulties for trustees if there is no income out of which to meet the costs of insurance.[62] The Law Reform Committee considered this point in some detail.[63] Nearly all of those who gave evidence to it considered that trustees should have a discretion to apportion the premiums to capital or income as they thought fit. We agree with this conclusion. **We provisionally recommend that trustees should have a discretion to apportion the payment of premiums between income and capital as they think fit and we ask whether readers agree.**

Application of the proposed powers and duties

9.27 Finally, we consider to which trusts these proposed powers and duties should apply. We consider that the proposed *power* to insure that we have set out in paragraph 9.18 above, should apply to all types of trust, whatever the nature of the property held, whether the trust is a private trust, a charitable trust or a pension trust, and whenever created, unless a contrary intention was expressed in the instrument creating the trust. In accordance with our stated policy of following the model of the Trustee Act 1925,[64] the powers of insurance that we propose would be additional to those conferred by the trust instrument.

9.28 A more difficult question is whether the limited *duty* to insure, that we have proposed in paragraph 9.21 above, should also apply—

(1) to all trusts whenever created, or only to those created thereafter; and

(2) where trustees insure under an express power in the trust instrument.

The Law Reform Committee "without pronouncing on the existing duties of trustees", took the view that it was unreasonable to impose a new duty of this kind upon trustees who might hitherto have been under no duty to insure.[65] Our provisional view is that the Law Reform Committee was unduly cautious. First, as we have explained, there is some reason to think that trustees may already be under a duty to insure where reasonable prudence demands it.[66] Secondly, we think it probable that trustees would in any event insure if they considered it prudent to do so. This is because, if readers agree with us, trustees would have the wide power to insure trust property that we have proposed. They would be expected to consider its exercise within a reasonable time of its having been granted and then from time to time thereafter.[67] One of the main criteria that the trustees would apply in determining whether to exercise it would be

[61] See above, para 9.4.

[62] In South Australia, the Trustee Act 1936, s 25(4) goes so far as to give trustees a power to borrow money to meet the premiums and to give the lender security over the trust property.

[63] The Powers and Duties of Trustees (1982) Cmnd 8733, paras 4.36, 4.37; see above, para 9.14, 9.15.

[64] Section 69(2); see above, paras 6.59, 6.60.

[65] *Ibid*, para 4.34. For the view that only professional trustees should be under a duty to insure, see Ann and Phillip Kenny, "The Underinsured Beneficiary" (1982) 79 LSGaz 755.

[66] See above, paras 9.4 and 9.10.

[67] This accords with the general obligation of trustees to consider whether or not to exercise their powers from time to time: see, eg *Re Hay's Settlement Trusts* [1982] 1 WLR 202, 210 (a case on powers of appointment, but the same principle applies to powers generally).

whether it was prudent to do so. Thirdly, we are not convinced that it is unreasonable to require trustees to act prudently. They are expected to do so in relation to their other powers and duties and if the position is otherwise in relation to insurance then it is anomalous. There must, in our view, be fairness to beneficiaries as well as to trustees. We would however emphasise that this is only a provisional view and one on which the views of readers would be particularly welcome.

9.29 **We provisionally recommend that—**

(1) the powers and duties which we propose in relation to insurance should apply to all trusts, whenever created, in addition to any powers conferred by the trust instrument; and

(2) the duty to insure which we propose in paragraph 9.21 above should also apply where trustees insure the trust property under an express power in the trust instrument.

In each case, this would be subject to any expression of contrary intention in the instrument creating the trust. Do readers agree with us? If not, would they explain what limitations they would place upon the applicability of the proposed powers and duties.

PART X
PROFESSIONAL CHARGING CLAUSES

INTRODUCTION

10.1 It has been the practice of trust draftsman for well over a century (and probably a great deal longer) to include as a matter of course a professional charging clause in any trust instrument. In its usual form, this clause authorises a trustee, who is engaged in any profession or business, to be paid out of the trust for all his or her reasonable fees and charges in respect of any business transacted on behalf of the trust, including any business which a non-professional trustee could have undertaken personally.[1] Given the almost universal inclusion of such clauses in trust instruments, it is at first sight rather puzzling that a statutory professional charging clause was not introduced as a default power long ago. Our primary concern in this Part is whether, as a matter of policy, a clause which permits professional trustees to charge for their services should be implied as a default provision. As we shall explain, the issues of policy have not in the past been regarded as clear-cut. We also address a number of defects in the law which applies to charging clauses, but these are subsidiary to this main question of policy. We begin with a brief statement of the relevant legal principles. We then examine the proposals of the Law Reform Committee when it considered this subject in 1983,[2] and explain why we are unable to agree with its conclusion that there should be no implied charging clause. We set out the case for reform and why we consider that professional trustees should be able to charge for their services in the absence of contrary provision in the instrument creating the trust. Finally, we recommend that the law should be changed so that they can, and we make other proposals for the reform of the law.

THE PRESENT LAW

The general rule and its exceptions

10.2 The present law can be summarised as follows. It was laid down long ago that "a trustee, executor, or administrator, shall have no allowance for his care and trouble".[3] This principle has often been repeated, and though it is subject to exceptions, it undoubtedly represents the present law.[4] Two reasons are traditionally given for the rule.[5] The first is that "a trustee is not allowed to derive a benefit from trust property".[6] The second is that to allow payment would place a trustee in a position where his or

[1] We explain the reasons for the particular elements of the clause below, para 10.5.

[2] 23rd Report, The Powers and Duties of Trustees (1982) Cmnd 8733, paras 3.42 - 3.55.

[3] *Robinson v Pett* (1734) 3 P Wms 249, 251; 24 ER 1049, *per* Lord Talbot LC.

[4] See, eg, *Re Barber* (1886) 34 ChD 77, 80; *Re Gee, dec'd* [1948] Ch 284, 293; *Re Worthington, dec'd* [1954] 1 WLR 526, 528; *Re Orwell's Will Trusts* [1982] 1 WLR 1337, 1340; *Re Duke of Norfolk's Settlement Trusts* [1982] Ch 61.

[5] For a different and rather fuller analysis, see W Bishop and D D Prentice, "Some Legal and Economic Aspects of Fiduciary Remuneration" (1983) 46 MLR 289. From an analysis of Lord Talbot's judgment in *Robinson v Pett*, above, they suggest that the non-remuneration rule can be justified on three grounds. These are "(a) without such a rule trustees would be tempted to abuse their position at the trust's expense; (b) the professional services of the individual trustee present acute valuation problems; and (c) trustees are free to refuse the office of trustee": *ibid*, at p 304.

[6] *Space Investments Ltd v Canadian Imperial Bank of Commerce Trust Co (Bahamas) Ltd* [1986] 1 WLR 1072, 1075, *per* Lord Templeman. See too *Re Barber*, above, at 80.

her interest and duty were in conflict—

> If it were not the rule, a trust estate might be heavily burdened by reason of business being done by a trustee or executor employing himself as commission agent for the estate.[7]

10.3 However, the rule has never been an inexorable one and there are a number of well-established exceptions to it.[8] These exceptions reveal that there is nothing inherently objectionable in remunerating trustees.[9] The point was made by Lord Normand in a well-known passage in *Dale v IRC*,[10] when he said that—

> it is not that reward for services is repugnant to the fiduciary duty, but that he who has the duty shall not take any secret remuneration or any financial benefit not authorized by the law, or by his contract, or by the trust deed under which he acts, as the case may be. In England,[11] moreover, the court has power to order payments to be made to trustees for whom the truster[12] has made no such provision, a power which it is difficult to reconcile with a general principle that remuneration is repugnant to trusteeship.

10.4 A trustee may be remunerated by way of exception to the general rule in a number of situations of which the following are the most important—

(1) *Where remuneration is authorised by the trust instrument*. Remuneration is usually authorised by means of a charging clause and the efficacy of such clauses is beyond doubt.[13] They are included almost invariably in trust instruments nowadays,[14] and are subject to a number of special rules that we consider in detail below.[15]

(2) *Where remuneration is sanctioned by statute*. There are a number of situations where a trustee is entitled to charge for his or her services by statute. These include[16] the following—

[7] *Re Barber*, above, at 81, *per* Chitty J; or as W Bishop and D D Prentice explain the matter, the rule prevents "overreaching in the form of generating unnecessary services": *op cit*, at 306.

[8] They are conveniently listed in David H Hayton, *Underhill and Hayton: Law of Trusts and Trustees* (15th ed 1995) p 639.

[9] Many other fiduciaries (such as agents) are remunerated as a matter of course.

[10] [1954] AC 11, 27.

[11] Although the appeal was an English one, Lord Normand was a Scottish Law Lord.

[12] Ie, settlor.

[13] See *Space Investments Ltd v Canadian Imperial Bank of Commerce Trust Co (Bahamas) Ltd* [1986] 1 WLR 1072, 1075. Their validity was established by the middle of the eighteenth century: see *Ellison v Airey* (1748) 1 Ves Sen 111, 115; 27 ER 924, 927.

[14] Thus in *Re Orwell's Will Trusts* [1982] 1 WLR 1337, 1340, Vinelott J commented that "[t]he harshness of the rule [which precludes a professional trustee from charging for his or her services] is normally if not invariably tempered in any well-drawn will or trust instrument by including an express charging clause".

[15] See paras 10.5 and following.

[16] The list is not comprehensive.

(a) where the court appoints a corporation (other than the Public Trustee) to act as trustee, it "may authorise the corporation to charge such remuneration for its services as trustee as the court may think fit";[17]

(b) where the court appoints a judicial trustee to act as trustee it may authorise the remuneration within certain prescribed limits;[18]

(c) where the Public Trustee acts as trustee;[19] and

(d) where the trustee is a custodian trustee.[20]

(3) *Where remuneration is authorised by the court*. The court has an inherent jurisdiction to grant trustees remuneration (or additional remuneration to that which the trust instrument allows).[21] It may do so either prospectively (for work that the trustees are likely to have to do)[22] or retrospectively (for work that has already been done).[23] The basis of the jurisdiction is to secure "the good administration of trusts".[24] In exercising its powers, the court will attempt to balance two factors.[25] The first is that trusteeship is gratuitous and that beneficiaries should therefore be protected against claims by trustees. The second is the great importance to the beneficiaries that the trust should be well administered. The court will, in particular, compare the value of the services of the trustees seeking remuneration against what it might cost the trust to obtain the equivalent from other trustees. The court will remunerate (or further remunerate) the trustees if, on balance, it would be in the interests of the beneficiaries to do so. Although it was said that the "jurisdiction should only be exercised sparingly, and in exceptional cases",[26] there are signs that the courts are more willing to allow remuneration than was formerly the case.[27] As we explain below, the Charity Commissioners have limited powers to authorise the remuneration of charity trustees.[28]

[17] Trustee Act 1925, s 42. In Northern Ireland, the court has a wider power so that it may "in any case in which the circumstances appear to it so to justify, authorise *any person* to charge such remuneration for his services as trustee as the court may think fit": Trustee Act (Northern Ireland) 1958, s 41. For a comment on this power, see Robert D Carswell, *Trustee Acts (Northern Ireland)* (1964) pp 96, 97 (suggesting that it would be used sparingly).

[18] Judicial Trustees Act 1896, s 1(5); Judicial Trustee Rules 1983, 1983 SI No 370, r 11. A judicial trustee tends to be appointed where the administration of a trust has broken down.

[19] Public Trustee Act 1906, s 9. For discussion, see David H Hayton, *Underhill and Hayton: Law of Trusts and Trustees* (15th ed 1995) pp 770 - 772.

[20] Public Trustee Act 1906, s 4(3). Those fees must not exceed those charged by the Public Trustee. For custodian trustees, see above, para 7.8.

[21] *Re Duke of Norfolk's Settlement Trusts* [1982] Ch 61.

[22] *Ibid*.

[23] *Foster v Spencer* [1996] 2 All ER 672.

[24] *Re Duke of Norfolk's Settlement Trusts*, above, at p 79, *per* Fox LJ.

[25] *Ibid*.

[26] *Re Worthington, dec'd* [1954] 1 WLR 526, 528, *per* Upjohn J.

[27] See *Re Duke of Norfolk's Settlement Trusts*, above; *Foster v Spencer*, above; N D M Parry "Remuneration of Trustees" [1984] Conv 275, 276.

[28] See para 10.13.

(4) *Where the court grants a fiduciary an allowance for skill and labour*. There is an ancient jurisdiction by which the court may in its discretion grant a fiduciary an allowance for his or her skill and labour where that person was liable to account for profits.[29] Although it has been suggested that this power is no more than a facet of the court's jurisdiction, explained in (3) above, to award remuneration to a trustee,[30] this is questionable, because they operate in different ways and are underpinned by different policy considerations.[31] In any event, the court's ability to grant such an allowance has been circumscribed by the House of Lords.[32] The jurisdiction will be exercised only exceptionally and not where it would encourage the trustees (or other fiduciaries) to place themselves in a position where their duty to the beneficiaries and their self interest were in conflict.[33]

(5) *When remuneration is by contractual arrangement with the beneficiaries*. Where the beneficiaries are of full age and capacity, and between them are absolutely entitled to the trust property, they may contract with the trustees to remunerate them.[34] The difficulty with such contracts is that they can only be supported by consideration if an intended trustee declines to act, or if a trustee who is already in post threatens to resign from the trust. Such conduct will often smack of either undue influence or equitable pressure and the contract may be set aside in consequence.[35]

(6) *When one of the trustees is a solicitor and undertakes litigation work for the trust*. This odd exception, usually known as the rule in *Cradock v Piper*,[36] permits a solicitor, who is one of two or more co-trustees, to charge his or her usual costs for work done in an action or matter in court on behalf of the trust, provided

[29] For an early case, see *Brown v Litton* (1711) 1 P Wms 140; 24 ER 329. The jurisdiction has been used primarily in the situation where one partner dies or resigns and the surviving partner(s) continue(s) running the business. It was codified by Partnership Act 1890, s 42. For a recent example, see *Popat v Shonchhatra* [1995] 1 WLR 908.

[30] *Re Berkeley Applegate (Investment Consultants) Ltd* [1989] Ch 32, 50 - 51. At p 51, Edward Nugee, QC, sitting as a deputy High Court Judge, spoke of "the underlying unity of the inherent jurisdiction which is exercised in such diverse circumstances".

[31] A trustee usually initiates proceedings for remuneration or additional remuneration. The court grants it if it considers it to be in the interests of the good administration of the trust. A claim for an allowance will generally arise in proceedings brought against a fiduciary, seeking an account, claiming a constructive trust, or seeking to set aside an agreement. It is an example of a court granting equitable relief to the claimant on terms that he or she recognises the contribution of the defendant fiduciary.

[32] *Guinness Plc v Saunders* [1990] 2 AC 663.

[33] *Ibid*, p 701.The House reached this conclusion without full consideration (or in some cases citation) of the authorities in which an allowance had been given to a fiduciary even though that person had profited from his or her fiduciary position, there had been a conflict of interest, or there had been some other inequitable conduct on his or her part. See *Re Macadam* [1946] Ch 73, 82; *Re Jarvis* [1958] 1 WLR 815, 819; *Phipps v Boardman* [1964] 1 WLR 993, 1018; *O'Sullivan v Management Agency and Music Ltd* [1985] QB 428, 467, 468, 472, 473.

[34] Where the trustees are already in post (and therefore bound by their duties under the trust) the consideration for such a contract will presumably be their willingness to continue as trustees rather than resign.

[35] See Lord Hardwicke's remarks in *Ayliffe v Murray* (1740) 2 Atk 58, 60; 26 ER 433, 434. For the doctrine of equitable pressure, see *Williams v Bayley* (1866) LR 1 HL 200.

[36] (1850) 1 Mac & G 664; 41 ER 1422.

that he or she has not added to the costs of the proceedings.[37] The anomalous nature of this exception has never been denied, but it is well established.[38] It even has its defenders.[39]

Charging clauses

10.5 There are a number of specific rules which apply to charging clauses. The first is that they are strictly construed against the trustee. Unless the clause is couched in very explicit terms, a professional trustee will be unable to charge for work which could have been undertaken by a lay trustee and did not require his or her professional expertise.[40] It has been said that a solicitor cannot insert a clause into a will (or presumably a trust) allowing him or her to charge for all work, unless expressly instructed to by his or her client.[41]

10.6 The second rule is that, for some but not all purposes, a trustee who is remunerated under a charging clause, is regarded as receiving a gift or legacy as a beneficiary under the will or trust,[42] and not as receiving payment for services rendered.[43] That has been held to be the case in the following situations—

(1) where the trust arose under a will which the trustee had attested, he was barred from receiving any remuneration,[44] because a gift or legacy to an attesting witness or his or her spouse was void under the Wills Act 1837;[45]

(2) for the purposes of legislation which imposed legacy duty, payments under the charging clause were regarded as a legacy;[46]

(3) where the testator's estate was insolvent, the right to charge was regarded as a

[37] See *Re Barber* (1886) 34 ChD 77, 81 - 83; *Re Corsellis* (1887) 34 ChD 675, 681, 682.

[38] For discussion of the rule, see A J Oakley, *Parker and Mellows: The Modern Law of Trusts* (6th ed 1994) p 534.

[39] For an interesting justification of the rule, see W Bishop and D D Prentice, "Some Legal and Economic Aspects of Fiduciary Remuneration" (1983) 46 MLR 289, 306. They state that the "primary justification for the non-remuneration rule is the difficulty of monitoring the payment that trustees award themselves in carrying out their trust obligations. Where, however, *Cradock v Piper* applies, these difficulties will be eliminated; the trustee's services will be visible and they are the type of services (unlike, for example, investment advice) that the court is uniquely qualified to cost".

[40] This states the effect of decisions such as *Re Ames* (1883) 25 ChD 72; *Re Chapple* (1884) 27 ChD 584; *Clarkson v Robinson* [1900] 2 Ch 722; *Re Chalinder & Herington* [1907] 1 Ch 58.

[41] "[U]nless the testator has expressly instructed him to insert those very words": *Re Chapple*, above, at p 587, *per* Kay J. We wonder how often that stricture is observed in practice.

[42] "The clause... is really a gift on condition. It is a gift of the privilege of charging, which the solicitor and trustee... would not otherwise have": *Re White* [1898] 1 Ch 297, 299, *per* Kekewich J.

[43] See the summary in *Re Duke of Norfolk's Settlement Trusts* [1982] Ch 61, 77.

[44] *Re Pooley* (1888) 40 ChD 1.

[45] Section 15.

[46] *Re Thorley* [1891] 2 Ch 613.

general legacy so that the trustee was not entitled to payment;[47]

(4) where there were insufficient assets to meet all legacies, the right to charge was regarded as a general legacy and abated proportionately.[48]

The origins of this characterisation of a charging clause as a gift or legacy go back to the mid-eighteenth century, and it was adopted, ironically, to overcome the objection that trusteeship should be unremunerated.[49]

10.7 For some purposes, payments to trustees for their services are not regarded as gifts or legacies. First, payment under a charging clause has been treated as "earned income" for the purposes of income tax legislation.[50] Secondly, where the court grants a trustee additional remuneration under its inherent jurisdiction, it is not varying a beneficial interest under the trust,[51] but is acting to secure the competent administration of the trust property.[52]

THE LAW REFORM COMMITTEE'S TWENTY-THIRD REPORT

No professional charging clauses

10.8 The issue of professional charging clauses was considered by the Law Reform Committee in its Twenty-third Report, The Powers and Duties of Trustees.[53] The Committee was opposed to the introduction of a general statutory charging clause as a default power despite the fact that a substantial majority of those from whom it took evidence favoured such a clause.[54] It gave three reasons for its conclusion—

(1) Settlors ought to be made aware both that a professional trustee would be remunerated and the terms of that remuneration. If a trust deed were drafted and it did not contain a charging clause because there was a statutory default clause, a settlor might not be conscious of what he or she had agreed to do.[55]

(2) It was concerned that "it would be difficult to frame a universally applicable provision which would not be open to abuse".[56]

[47] *Re White* [1898] 1 Ch 297 (Kekewich J, where the facts are fully stated); [1898] 2 Ch 217 (CA). There were insufficient sums to pay all the debts of the deceased's estate in full. If the trustee had been able to claim his remuneration as a debt to the estate, he would have recovered part of it.

[48] *Re Brown* [1918] WN 118.

[49] See *Ellison v Airey* (1748) 1 Ves Sen 11, 115; 27 ER 924, 927, where Lord Hardwicke LC swept aside an objection to a charging clause by saying "this was a legacy to the trustees; to whom the testator may give this satisfaction, if he pleases".

[50] *Dale v IRC* [1954] AC 11. Lord Normand commented that "[t]here need be no incompatibility in saying that the income is a conditional gift of the testator but that it has to be earned by compliance with the testator's condition of serving as a trustee": *ibid*, at p 28.

[51] Which could only be done under the Variation of Trusts Act 1958 or under the very limited inherent "salvage" jurisdiction to vary trusts established in *Chapman v Chapman* [1954] AC 429.

[52] *Re Duke of Norfolk's Settlement Trusts* [1982] Ch 61, 78.

[53] (1982) Cmnd 8733, paras 3.42 - 3.55. For a valuable commentary on these specific proposals to which we are indebted, see N D M Parry, "Remuneration of Trustees" [1984] Conv 275.

[54] (1982) Cmnd 8733, paras 3.46, 3.47.

[55] *Ibid*, para 3.47.

[56] *Ibid*.

(3) To make such clauses standard would "encroach too far upon the general principle that a trustee should not profit from his trust and is likely to be inappropriate in certain cases, for example charitable trusts".[57]

These reasons have been criticised,[58] and we are not persuaded by them for the reasons that we explain in the following paragraphs.

10.9 First, if a trust does not contain a charging clause, no professional trustee is likely to be willing to administer the trust. This may be to the detriment of the trust, and may mean (in particular) that the beneficiaries under home-made wills are thereby penalised. The outcome may be either that a costly application has to be made to the court to appoint a corporate trustee which will in practice be authorised to charge for its services,[59] or that the Public Trustee (who has a statutory duty to charge for her services) will be appointed.[60] In either eventuality, the trust will have to pay for the services of a professional trustee and those sums may be more than if, say, a local solicitor or accountant was employed to do the work.

10.10 Secondly, even if a trustee is appointed who is not a professional, he or she may both delegate much of the administration of the trust to and pay a professional agent, even if the work *could* be done by the trustee.[61] This is so in regards to many matters under the present law, and more functions will become delegable if the proposals on delegation contained in Part VI of this Report are accepted. Settlors cannot, in other words, expect to have their trusts administered without cost. Furthermore, we have explained in Part II of this Paper that the proper administration of trusts increasingly requires recourse to the services of those with professional expertise in investment or property management. One way of meeting this need is to widen trustees' powers of delegation (as we have proposed). Another is to facilitate the employment of trustees with the appropriate expertise.

10.11 Thirdly, it is now common in express professional charging clauses to include a provision that the charges—

(1) shall be reasonable; and

(2) shall not exceed the normal professional fees that would be charged for that work by that person.

There is therefore a yardstick by which professional charges can be tested. Furthermore, we have made informal inquiries as to whether there is any evidence of abuse by solicitor trustees,[62] and these have suggested that in practice there is very

[57] *Ibid*.

[58] See N D M Parry, "Remuneration of Trustees" [1984] Conv 275. As we mention, there are a number of inconsistencies in the reasons given by the Committee for its different recommendations.

[59] Under Trustee Act 1925, s 42, above, para 10.4(2)(a).

[60] Public Trustee Act 1906, s 9; above, para 10.4(2)(c).

[61] The Law Reform Committee accepted this point, and it influenced another of their recommendations: see The Powers and Duties of Trustees (1982) Cmnd 8733, para 3.45.

[62] Taking that profession simply as a paradigm.

little.[63] We shall be glad to learn from readers whether they have had any experience of excessive charging by professional trustees in cases where the fact of excessive charging was subsequently either verified or accepted by the trustee.[64]

10.12 Fourthly, the rule against a trustee profiting from his or her trust has never been an absolute rule.[65] As we have explained above,[66] the authorised remuneration of trustees is not regarded as repugnant to the nature of trusteeship.[67] It is the unauthorised receipt of secret payments that is regarded as unacceptable. Given the widespread use of professional charging clauses, remuneration is regarded as the norm.

10.13 Finally, the Charity Commissioners will register a charity when it is being set up even if the trusts make provision for the remuneration of the trustees, provided that the nature and level of remuneration is tied to the services undertaken by the trustees and the remuneration is limited to a reasonable sum for the services performed.[68] The position is much more difficult in relation to existing charities. The Commissioners do have a limited power to authorise remuneration in individual cases. This they exercise in accordance with the guidelines laid down by the courts when sanctioning remuneration for trustees,[69] that is to say, where "it can be shown to be both necessary and reasonable in the interests of the charity".[70] We explain below that there may be special considerations that justify treating charitable (and pension) trusts differently from other trusts.[71]

Attesting witnesses and charging clauses

10.14 The Law Reform Committee was also opposed to changing the rule that where a person (or his or her spouse) witnessed a will, they could not receive any remuneration under a professional charging clause contained in that will.[72] The reason given was that—

> [i]t lies within the discretion of the testator whether or not a charging

[63] We are very grateful to the Office for the Supervision of Solicitors for their assistance on this point.

[64] In relation to a solicitor who acts as the only personal representative of a deceased's estate, a residuary beneficiary can seek a remuneration certificate in respect of the costs of the work undertaken: see Solicitors' (Non-Contentious Business) Remuneration Order 1994, SI 1994 No 2616. This is not available in cases where the solicitor acts as trustee, but his or her costs may be taxed. We are grateful to the Office for the Supervision of Solicitors for drawing this point to our attention.

[65] See *Ellison v Airey* (1748) 1 Ves Sen 111, 115; 27 ER 924, 927.

[66] Para 10.3.

[67] *Dale v IRC* [1954] AC 11, 27.

[68] (1994) 2 *Decisions of the Charity Commissioners*, p 15. The trust must be established for purposes which are exclusively charitable, and this will not be so if the remuneration is not tied to the services which the trustees perform.

[69] (1994) 2 *Decisions of the Charity Commissioners*, pp 16 - 20. For the court's powers, see above, para 10.4(3).

[70] (1994) 2 *Decisions of the Charity Commissioners*, p 15.

[71] See para 10.28.

[72] The Powers and Duties of Trustees (1982) Cmnd 8733, paras 3.48, 3.49. For this rule, see above, para 10.6(1).

> clause is included in the will, so that if one is included it must necessarily count as bounty and should not therefore be paid if the solicitor has witnessed the will.[73]

That view is of course consistent with the traditional view that we have explained, that a charging clause is to be treated as a conditional gift for most purposes.[74] However, in another of its recommendations, the Committee proposed that amounts due under a charging clause should be regarded as administration expenses and not, as at present, as general legacies. They would therefore rank in priority to general legacies and would be paid even if the estate would otherwise be exhausted by specific legacies.[75] It is not easy to see why, if an amount due under a charging clause should be regarded as an expense of administration for this purpose, it should not also be similarly regarded for the purposes of the rule against attesting witnesses.

10.15 The other main proposals by the Committee can be briefly mentioned. First, it recommended that in those comparatively rare cases where a professional person applies to act as an administrator,[76] he or she could be authorised by the court to charge for his or her services on that person's application for a grant of administration.[77] As the law stands, an administrator is entitled to no remuneration unless either—

(1) all those entitled under the deceased's estate are of full age and capacity and agree to such payment; or

(2) the court grants him or her remuneration under its inherent jurisdiction.[78]

10.16 Finally, the Committee recommended that where there was a professional charging clause, a professional trustee should be entitled to charge for work which could have been done by a lay trustee.[79] This would be achieved by means of a presumption.[80] This would have the effect of reversing the strict rule of construction that presently

[73] *Ibid*, para 3.49.

[74] See above, para 10.6.

[75] The Powers and Duties of Trustees, above, paras 3.44, 3.45. This would alleviate the problems explained above, paras 10.6(3) and (4). For discussion, see N D M Parry, "Remuneration of Trustees" [1984] Conv 275, 278 - 280.

[76] The administrator of an intestate's estate will normally be a member of his or her family: see Non-Contentious Probate Rules 1987, 1987 SI No 2024, r 22 (which sets out the order of priority for a grant of administration). A professional person could be appointed where there was an application under Supreme Court Act 1981, s 114(2) (grants in cases of an infant beneficiary or where a life interest arises), or (4) (where there is an infant beneficiary or a life interest and there is only one administrator, not being a trust corporation).

[77] The Powers and Duties of Trustees, above, paras 3.53, 3.54.

[78] See *Re Worthington, dec'd* [1954] 1 WLR 526, where Upjohn J, in refusing the application, held that such remuneration would be granted sparingly and only in exceptional circumstances: *ibid*, at p 528. A court might not take such a restricted view of the jurisdiction after *Re Duke of Norfolk's Settlement Trusts* [1982] Ch 61. See above, para 10.4(3).

[79] The Powers and Duties of Trustees, above, paras 3.51, 3.52.

[80] A charging clause would presumably have to state explicitly that the professional trustee could *only* charge for work requiring professional expertise and for no other to rebut the presumption.

applies to such clauses.[81]

THE CASE FOR REFORM

The issues

10.17 The case for reform falls into two parts. The first concerns the fundamental question of principle: should all trustees, executors and administrators who are professionals have power to charge for the work which they undertake on behalf of the trust or estate if there is neither any provision for remuneration (or any other benefit) nor a direction to the contrary in the trust instrument or will? The second concerns points of detail where the existing law is unsatisfactory.

Should there be a statutory charging clause?

10.18 We consider that the case for a statutory charging clause is a strong one. First, as we have emphasised in Part II of this Paper, the administration of trusts nowadays often requires professional skills. One solution to this problem is to give wider powers of delegation (as we have proposed in Part VI). Another solution is to make it easier to employ professional trustees who have the required skills or access to them. Secondly, and following from this, although many trusts will be able to employ a professional trustee because they contain an express charging clause, there will be many others that cannot because they do not have such a power. The obvious cases are trusts arising under home-made wills, trusts arising on an intestacy, and older trusts (such as charitable trusts). Two examples may be given of the sort of problems that may arise where the trust does not contain a charging clause. The first is when a trustee of a small family trust wishes to retire and no one is willing to take on the task. To overcome the problem, either the trust will have to incur the expense of an application to the court to appoint a corporate trustee (who can and normally will be remunerated), or the Public Trustee (who has a statutory duty to charge) will have to be appointed.[82] Neither of these may be the most appropriate course for a small trust. The second example is where a charity needs the expertise of a professional trustee to assist in the day-to-day running of the trust. The trustees may be unable to obtain the necessary expertise if they cannot remunerate the professional.[83] There are other incidental advantages in having a statutory charging clause. For example, it will shorten trust deeds and wills as such clauses are now included as a matter of course.[84]

10.19 The objection to charging clauses is rooted in the now out-dated view that—

> this court looks upon trusts as honorary, and a burden upon the honour and conscience of the person intrusted, and not undertaken upon mercenary views...[85]

We agree with one commentator that—

[81] See above, para 10.5.

[82] See above, para 10.9.

[83] However, as we explain below, there may be countervailing considerations in relation to charitable trusts which make the automatic implication of a professional charging clause undesirable: see para 10.28.

[84] This point was specifically mentioned to us by a practitioner.

[85] *Ayliffe v Murray* (1740) 2 Atk 58, 60; 26 ER 433, 434, *per* Lord Hardwicke LC.

> [i]t is time to recognise that the changed social and economic circumstances in which trusts today operate call for increasing professionalism on the part of trustees. If a professional is appointed to undertake this function, which the [Law Reform] Committee itself describes as an 'onerous one' then he should be entitled to reasonable remuneration for his services.[86]

We also agree with his view that the Law Reform Committee may have been "too cautious" in its proposals.[87] In any event, the social and economic environment within which trusts must now operate has changed significantly since the Committee reported in 1982.[88] We note that in the United States of America "[t]here are statutes in almost all the of the states that make provision for the compensation of trustees",[89] and in Australia, several states have statutory charging clauses.[90]

Other defects in the law

10.20 There are two other specific difficulties with the present law that should, in our view be addressed. The first is that payments under professional charging clauses are treated for many (but not all) purposes as a gift or "bounty". The reasons for this are largely historical and are closely related to the outmoded view of trustees as "gentlemen amateurs" that we have explained in the previous paragraph. Such payments are remuneration for services rendered and should, in our view, be treated as such.[91] If that is done, a number of problems which presently arise in relation to such clauses and which we have identified,[92] fall away. The second difficulty is the strict construction that is given to charging clauses in an attempt to limit them to work which requires the services of a professional. It is in practice very difficult "to draw the line between professional and non-professional work".[93] It may also be counter-productive because it discourages professionals from acting as trustees. The evidence received by the Law Reform Committee showed that professional trustees were unlikely to accept a trusteeship unless they were remunerated for *all* the work that they undertook for the trust, whether or not that work could have been done by a lay person.[94]

[86] N D M Parry, "Remuneration of Trustees" [1984] Conv 275, 285. See to similar effect, W Bishop and D D Prentice, "Some Legal and Economic Aspects of Fiduciary Remuneration" (1983) 46 MLR 289, 304.

[87] N D M Parry, "Remuneration of Trustees", above, at p 285.

[88] See Part II of this Paper.

[89] W F Fratcher, *Scott on Trusts* (4th ed 1987) §242.

[90] See, eg, Queensland Trusts Act 1973, s 101(2) which provides that "[i]n the absence of a direction to the contrary in the instrument creating the trust, a trustee, being a person engaged in any profession or business for whom no benefit or remuneration is provided in the instrument, is entitled to charge and be paid out of the trust property all usual professional or business charges for business transacted, time expended, and acts done by him or his firm in connection with the trust, including acts which a trustee not being in any profession or business could have done personally". See too the Western Australian Trustee Act 1962, s 98(5).

[91] We do not wish to call into question in any way the widespread practice by which testators leave legacies in their wills to their executors. Our concern is *only* with professional charging clauses.

[92] See above, para 10.6.

[93] Law Reform Committee, 23rd Report, The Powers and Duties of Trustees (1982) Cmnd 8733, para 3.51.

[94] *Ibid*.

PROPOSALS FOR REFORM

Statutory charging clause

10.21 In the light of this analysis we consider that there should be an implied statutory charging clause which would enable professional trustees to charge for their services. The clause we propose follows the form that is widely used in trust instruments and in legislation in other jurisdictions. We have four concerns which we have attempted to address.

10.22 First, we are aware of the need to ensure that beneficiaries are protected against trustees who seek to overcharge for their services. To that end, we consider that charges should not only be limited to what is reasonable,[95] but that they should not exceed the charges which the professional trustee would charge for those services in the course of his or her business or profession.[96]

10.23 Secondly, we have felt some unease about the applicability of our proposed clause to pension trusts and charitable trusts, given the special nature of each. We have therefore decided to offer a wider range of options in relation to such trusts which we explain below.[97]

10.24 Thirdly, we do not consider it appropriate that the power should apply where the trust instrument confers some other benefit or remuneration on the trustee or trustees. Nor should it apply where there is a contrary direction in the instrument. However, a term which limited the remuneration of one or more of the trustees in some way would not for these purposes be regarded as a direction to the contrary.[98]

10.25 Finally, a particular difficulty arises where the court[99] has already authorised the payment of a trustee for work that has been done or which is in contemplation.[100] We would not wish that fact to exclude the application of the power to that trust or estate for the future. However, we consider that it would be wrong in principle for the trustees or personal representatives to be further remunerated for the particular work beyond what had already been allowed by the court. Once that specified work was completed, any charge for further work by a professional trustee would be pursuant to the proposed statutory power.

10.26 **We provisionally recommend that there should be an implied statutory charging clause and that it should apply—**

(1) in relation to all trusts (other than charitable trusts and pension trusts) and to the unadministered estates of all deceased persons except—

[95] A concept that is somewhat elusive.

[96] This should be readily ascertainable as a matter of evidence by reference to the basis on which the trustee charges when acting in the course of business.

[97] See para 160.

[98] Our attention has been drawn to the fact that in charitable trusts there are commonly provisions which limit the level of remuneration in some way. These are included to meet the concerns of the Charity Commissioners and their purpose is to ensure that the charitable status of a trust is not imperilled.

[99] Or, if our proposals are to apply to charitable trusts, the Charity Commissioners.

[100] See above, paras 10.4(3) (powers of the court); 10.13 (Charity Commissioners).

(a) where there is a direction to the contrary in the will or trust instrument (but not merely some limitation on remuneration); or

(b) where some other benefit or remuneration is provided in the will or trust instrument;

(2) whether the trust arose or the deceased person died before or after any legislation was brought into force; and

(3) notwithstanding, but subject to, any previous order by a court[101] which has authorised the trustees or personal representatives to be remunerated for any work.

10.27 **We provisionally recommend that—**

(1) the charging clause should permit any trustee or personal representative who is also engaged in a profession or business to charge and be paid out of the trust property for any business or act done, advice given, or time expended in connection with the trust;

(2) the power to charge in (1) should apply whether or not the matter was one which a trustee not being a professional could have undertaken; and

(3) those charges should be reasonable and should not exceed the amount which the trustee would charge for such work in the ordinary course of his or her business or profession.

We ask whether readers agree with our proposals for a default power in principle. If they do, we should like to know whether they agree with the detailed terms which we propose for it, or whether they consider that those should be modified and if so, in what respects.

10.28 We have special concerns about pension trustees and charity trustees. The position of pension trustees has been the subject of detailed recent legislation.[102] A statutory charging clause could cut across the provision that has been made for pension trustees[103] and might in any event be inappropriate for trusts of that kind. There are also special factors which affect charity trustees. In particular, the Charity Commissioners have pointed out that "charities exist for the public benefit. Persons administering charities must act altruistically and not for their own benefit".[104] Furthermore, in the case of charitable trusts, it may be more difficult to prevent overcharging by the trustees who are not subject to the vigilant eyes of beneficiaries. In these circumstances, we consider that there are three possible options in relation to

[101] Or, if the proposals apply to charitable trusts, by the Charity Commissioners.

[102] See Pensions Act 1995, Part I.

[103] See, eg, Pensions Act 1995, ss 42, 43, which make provision for the attendance of employee trustees at trustees' meetings and provide that they must both have time off work to attend and be paid by their employer while attending.

[104] (1994) 2 *Decisions of Charity Commissioners*, 14.

each form of trust. **We ask readers whether, in relation to—**

(1) pension trusts; and

(2) charitable trusts;

the statutory charging clause that we have proposed—

(a) should apply;

(b) should be wholly inapplicable; or

(c) should not apply automatically, but the trustees should have power to authorise one (or more) of their number to charge for his or her services in accordance with the clause?

Other reforms

10.29 We have already indicated that we do not consider it appropriate that a charging clause (whether express or implied under our proposed statutory clause) should continue to be regarded as a form of "bounty", so as to be treated for many purposes as a legacy or gift.[105] Our proposal is that it should be regarded as remuneration for work done. In relation to the administration of a deceased's estate (where the point matters in practice), the charges would be an expense of administration and would therefore have priority over legacies and other debts of the deceased,[106] which is not the case at present.[107] Because this proposal would affect the priority of claims, we consider that it should not be retrospective, because it might divest persons entitled under the deceased's estate of their vested rights.[108]

10.30 **We provisionally recommend that—**

(1) a charging clause should no longer be regarded as a conditional gift or legacy but as remuneration;

(2) any sum due under such a clause should be an expense of administering the trust or estate;

(3) this proposal should only apply to trusts created or to the estates of persons dying after any legislation which implemented these recommendations was brought into force.

[105] See above, para 10.20.

[106] See J H G Sunnucks, J G Ross Martyn and K M Garnett, QC, *Williams, Mortimer and Sunnucks on Executors, Administrators and Probate* (17th ed 1993) p 633.

[107] See above, para 10.6.

[108] To make the provision retrospective might contravene Article 1 of the First Protocol of the European Convention for the Protection of Human Rights and Fundamental Freedoms, which provides that "[e]very natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law". The Article has been widely interpreted by the European Court of Human Rights.

We ask whether readers agree with us.

10.31 If these proposals were accepted, one statutory provision and one rule of common law would be rendered obsolete. First, the court would no longer need the statutory power[109] to authorise a corporation that it had appointed as trustee to charge for its services. It could therefore be repealed. Secondly, the anomalous rule by which a solicitor trustee can charge for litigation work[110] would be redundant. We doubt that its formal abrogation would be necessary: the rule would simply be subsumed in the wider statutory power.

10.32 Finally, we consider that the rules by which express charging clauses are strictly construed against the professional trustee and confined to activities which require a professional unless the contrary is clearly expressed[111] should be abrogated. This is consistent with the widespread use of such clauses and with our proposal that there should be a statutory charging clause. **We provisionally recommend that—**

(1) a professional charging clause should be taken to permit a trustee to charge for work and services properly rendered for the trust, whether or not that work or those services could have been provided by a lay trustee, unless the trust instrument provides to the contrary; and

(2) this provision should apply to all professional charging clauses in wills and trusts, whenever made.

We ask whether readers agree with us.

[109] Under Trustee Act 1925, s 42; see above, para 10.4(2)(a).

[110] The so-called rule in *Cradock v Piper* (1850) 1 Mac & G 664; 41 ER 1422; above, para 10.4(6).

[111] See above, para 10.5.

PART XI
SUMMARY OF ISSUES FOR CONSULTATION

INTRODUCTION

11.1 In this Part we summarise the issues on which we seek the views of readers. Some readers may not wish to comment on all issues: their remarks are no less welcome. We would also be grateful for comments not only on the matters specifically listed below, but on any other points raised by this Paper. It would be very helpful if, in responding, readers could indicate either the paragraph of the summary that follows to which their remarks relate, or the paragraph of the Paper.

APPLICABILITY

11.2 Do you agree that the proposals contained in this Paper should apply to—

(1) all trustees;

(2) personal representatives; and

(3) to directors of charitable corporations to the extent that they apply to charity trustees;

except where it is otherwise stated or where the context otherwise requires?

(Paragraph 1.19)

POWERS OF COLLECTIVE DELEGATION

Should trustees' powers of collective delegation be reformed?

11.3 Do you agree with our view that the law on trustees' powers of collective delegation should be reformed? If not, can you explain why you think that the present law should remain unchanged?

(Paragraph 6.2)

The proposed new power to delegate

11.4 Our provisional view is that, subject to any expression of contrary intention in the trust instrument, trustees—

(1) should have authority to delegate to agents their powers to administer the trust, including their powers of investment and management; but

(2) should have no authority to delegate their powers to distribute the income or capital of the trust for the benefit of its objects, except in relation to trust property abroad.

The power to delegate under (1) could either be in relation to a specific act or acts, or by way of a general retainer. It should remain the case that the matters delegated were ones that were required to be done in the execution of the trust or the administration

of a deceased's estate. There should be no requirement that the delegation should be made by power of attorney.

11.5 These recommendations would be without prejudice to—

(1) the power of an individual trustee to delegate all or any of his or her trusts, powers and discretions under section 25 of the Trustee Act 1925; or

(2) the need to comply with any conditions laid down by law or by the instrument creating the trust in relation to the exercise of any power of investment or management.

11.6 Do you agree with our proposal for a new broad power of delegation and the terms on which it is given? Do you think that the distinction which it draws between the administration of the trust and the distribution of trust property is the right one, or would you prefer some other distinction?

(Paragraphs 6.26, 6.27 and 6.29)

Conditions for exercising the power

11.7 Our provisional view is that—

(1) trustees should review any delegation of their functions at regular intervals; and

(2) trustees who wished to delegate the powers of management specified in the following paragraph should be required to—

(a) consider the appropriateness of any such delegation before making it;

(b) draw up and review at reasonable intervals a written statement of their policy in relation to the exercise of the powers delegated which reflected their fiduciary obligations to ensure that the trust was administered in the best interests of the objects of that trust;

(c) inform the agent of that policy; and

(d) take reasonable steps to ensure that he or she both complied with it and reported back to the trustees at regular intervals as to its execution.

11.8 The requirement in paragraph 11.7 would apply to the following powers—

(1) to select investments;

(2) to sell, lease, or charge trust property;

(3) to grant options or rights of pre-emption over trust property; or

(4) to acquire property for the benefit of the trust.

(Paragraphs 6.31, 6.32)

11.9 Do you agree with our proposals and, in particular, do you consider that—

(1) any powers should either be added to or removed from the list in the preceding paragraph; or

(2) any other restrictions or conditions should be imposed.

(Paragraph 6.33)

11.10 Do you agree that the existing statutory provisions that confer powers on trustees to pay agents and to be reimbursed for their own expenses incurred in the execution of their duties should be replaced by a provision that would make it clear that trustees were authorised to pay only the *reasonable* fees of their agents and to be reimbursed only for expenditure *reasonably* incurred by themselves?

(Paragraph 6.34)

Specific delegation powers

11.11 Do you agree with our provisional view that trustees should have power—

(1) to authorise their agents to employ sub-agents; and

(2) to employ agents on terms which limit their liability;

provided that it was reasonably necessary for the trustees to do so? (For these purposes, an act would be reasonably necessary if an ordinary prudent person would have done it.)

(Paragraph 6.37)

11.12 Do you consider that trustees—

(1) should not be permitted to sanction actual or potential conflicts of interest by their agents in the absence of express authority in the instrument creating the trust; or

(2) should have power to authorise conflicts of interest by their agents—

(a) if it was reasonably necessary to do so; and/or

(b) if it was it was in the reasonable opinion of the trustees in the best interests of the trust; and/or

(c) in some other circumstances or if some other conditions were satisfied, and if so, in what circumstances or conditions?

If you favour (2), do you consider that the requirements in (a), (b) and (c) should be alternative or cumulative?

(Paragraph 6.39)

11.13 Our provisional view is that trustees should be permitted to delegate collectively a function to one or more of their own number whenever they might have delegated it to an agent and subject to the same restrictions. The trustee-agent would be entitled

to recover—

(1) any expenses reasonably incurred in performing the agency; and

(2) if he or she were acting in pursuance of a profession or business, all usual professional or business charges reasonably incurred.

Do you agree with all or part of this proposal? You are invited to consider this issue in conjunction with the provisional proposals in paragraphs 11.45 and 11.46 below.

(Paragraph 6.42)

Duties of care

11.14 Our provisional view is that there should be one standard of care expected of trustees in relation to delegation under the powers which we have proposed above and that it should apply to each of the following matters—

(1) the selection of any agent;

(2) the terms on which the agent is employed; and

(3) the supervision of that agent once appointed.

Do you agree with this proposal, and if not what matters do you think should be subject to any duty of care?

(Paragraph 6.45)

11.15 Do you think that trustees who delegate their discretions to one or more of their own number should be vicariously liable for the acts of the trustee delegates, whatever the standard of care that should otherwise be applicable in relation to powers of delegation?

(Paragraph 6.50)

11.16 Should the standard of conduct expected of trustees when delegating be that they should—

(1) act in good faith;

(2) be vicariously liable for all the acts and defaults of their agents;

(3) be required to satisfy a series of specified criteria, compliance with which would be a defence to any proceedings;

(4) be required to act with the care of the ordinary prudent person of business; or

(5) act with the care and diligence that may reasonably be expected having regard to the nature, composition and purposes of the particular trust, the skills which the trustees actually have, or if they are employed as professional trustees, those which they either ought to have or hold themselves out as having?

If you favour option (3) we would be grateful for suggestions as to what you think the

criteria might be.

(Paragraph 6.55)

11.17 Our provisional view is that the same standard of care that is thought to be appropriate in relation to the proposed statutory power of delegation should apply equally to any express power to delegate conferred by the instrument creating the trust unless some other standard is expressly or impliedly specified in that instrument. Do you agree?

(Paragraph 6.56)

Application of the new power

In general

11.18 Our provisional view is that—

(1) any new power of delegation should apply to trusts in existence when any legislation is brought into force as well as to trusts created thereafter; and

(2) a provision having the same effect as section 69(2) of the Trustee Act 1925 should apply to any new power of delegation so that it would be inapplicable if a contrary intention was expressed in the instrument creating the trust.

Do you agree, or do you consider that the power should be either more or less limited in its application?

(Paragraphs 6.58, 6.60)

11.19 Do you agree that where a trust has previously been granted additional powers to delegate by the court or the Charity Commissioners, it should have the benefit of the new statutory powers as well?

(Paragraph 6.61)

Charitable trusts

11.20 Do you agree with our provisional view that charity trustees—

(1) should have power to delegate matters which relate to income generation even though this entails the delegation of their discretions; but

(2) should have the same powers as they have at present to delegate all other matters relating to the execution of the trusts so that they can only delegate functions which are purely ministerial?

If you disagree, what principles would you apply to charity trustees?

(Paragraph 6.65)

11.21 We provisionally recommend that charity trustees should have power to delegate the following functions—

(1) all matters relating exclusively to the investment of trust property (real or personal), including powers—

(a) to manage such property;

(b) to sell or lease trust property (whether at a fixed price or at a consideration to be fixed by valuation); and

(c) to acquire property for the trust (whether at a fixed price or at a consideration to be fixed by valuation);

(2) all matters relating to the raising of funds for the charity; and

(3) any acts of a ministerial character which are concerned with the administration of the charity;

but no others, unless expressly authorised by the Charity Commissioners.

Do you agree with all or any part of this list of functions? What amendments, additions or deletions (if any) would you wish to make to it?

11.22 Our provisional view is that all other restrictions and limitations that we propose in relation to the power set out in paragraph 11.4 above, would apply equally to these powers with necessary modifications. Do you agree?

(Paragraphs 6.67, 6.68)

11.23 We provisionally recommend that, subject to the provisions of the Pensions Act 1995 regarding the delegation of investment decisions, trustees of occupational pension schemes should have the wide powers of delegation proposed in paragraph 11.4, with necessary modifications to take account of the overriding nature of section 34 of the Pensions Act 1995. Do you agree, or do you think that there should be restrictions on the powers of such trustees to delegate their non-investment functions? If so, what should those restrictions be?

(Paragraph 6.70)

POWERS TO EMPLOY NOMINEES AND CUSTODIANS

The powers proposed

11.24 Do you agree with our view that—

(1) trustees should have a power to vest trust assets in the name of a nominee, provided that such person acts as a nominee in the course of its business, and that for these purposes, "trust assets" should be widely defined to include both choses in action and any legal or equitable property rights that the trust might

have; and

(2) the effect of employing a nominee under this power should be stated in statutory form so as to make it clear that—

(a) the nominee would hold the property to the order of the trustees in accordance with the terms agreed between the parties; and

(b) the trustees would hold the benefit of their rights against the nominee on the applicable trusts?

11.25 Do you agree that trustees should have a power to deposit trust documents (whether of title or otherwise) or trust property with a custodian for safe keeping, provided that such person is a custodian in the course of its business, and that this power would be without prejudice to the existing right of trustees to leave trust documents in the custody of one of the trustees?

11.26 If you support the proposed powers set out in the two preceding paragraphs, do you consider that trustees who employ a nominee or custodian under them should be under an obligation to review the employment at reasonable intervals as a safeguard to beneficiaries, or do you think that such an obligation is either unnecessary or should be more restricted in some way?

(Paragraphs 7.19 - 7.22)

11.27 We provisionally recommend that trustees should have—

(1) power to pay custodians and nominees their reasonable fees;

(2) power where it is reasonably necessary to do so—

(a) to authorise the nominee or custodian to sub-delegate any of its functions to a sub-nominee or sub-custodian; and

(b) to employ nominees and custodians on terms which limit their liability; and

(3) discretion to allocate the costs of employing a nominee or custodian between income and capital.

Do you agree? (For these purposes, an act would be reasonably necessary if an ordinary prudent person would have done it.)

(Paragraphs 7.24, 7.25)

11.28 Do you agree with our recommendation that there should be no power for trustees to vest trust property in one or some of their number as nominees in the absence of express authorisation in the instrument creating the trust?

(Paragraph 7.26)

11.29 We provisionally recommend that trustees should have power to acquire and to hold

property for the trust jointly or in common with other persons. Do you agree?

(Paragraph 7.27)

Protection for beneficiaries

11.30 Do you agree with our provisional view that, subject to the special position of charities, there should be no restrictions on the bodies that trustees might employ as nominees or custodians under the proposed power?

(Paragraph 7.32)

11.31 Do you consider that there should be statutory restrictions on the nominees which may be employed by charitable trusts to ensure a higher degree of protection for the trust fund?

(Paragraph 7.33)

11.32 Our provisional view is that trustees should not be given a default power to insure against loss caused by the acts, neglects and defaults of any nominee or custodian which they employed. Do you agree?

(Paragraph 7.35)

11.33 Do you agree that there should be one standard of care expected of trustees in relation to the employment of nominees and custodians under the powers which we have proposed and that it should apply to each of the following matters—

(1) the selection of any nominee or custodian;

(2) the terms on which that person is employed; and

(3) the supervision of that person once appointed?

11.34 Should the standard of conduct expected of trustees when appointing and controlling a nominee or custodian be that they should—

(1) act in good faith;

(2) be vicariously liable for all the acts and defaults of their nominee or custodian;

(3) be required to satisfy a series of specified criteria, compliance with which would be a defence to any proceedings;

(4) be required to act with the care of the ordinary prudent person of business; or

(5) act with the care and diligence that may reasonably be expected having regard to the nature, composition and purposes of the particular trust, the skills which the trustees actually have, or if they are employed as professional trustees, those which they either ought to have or hold themselves out as having?

11.35 Our provisional view is that the same standard of care that is thought to be appropriate

in relation to the proposed statutory power to employ nominees and custodians should apply equally to any express power to employ such persons conferred by the instrument creating the trust unless some other standard is expressly or impliedly specified in that instrument. Do you agree?

(Paragraphs 7.37, 7.38 and 7.40)

11.36 We provisionally recommend that the proposed powers to employ nominees and custodians should apply—

(1) to trusts created whether before or after any legislation was brought into force unless a contrary intention was expressed in the instrument creating the trust; and

(2) to all types of trust, including charitable and pension trusts, subject to the one qualification set out in paragraph 11.31 above.

Do you agree?

(Paragraphs 7.41, 7.42)

POWER TO PURCHASE LAND

11.37 We provisionally recommend that—

(1) all trustees (other than trustees of land and trustees of the settlement under the Settled Land Act 1925[1]) should have power to purchase a legal estate in land in England or Wales;

(2) trustees should be able to exercise that power—

(a) by way of investment;

(b) for occupation by any beneficiary; or

(c) for any other means; and

(3) when exercising this power, should be able to do so with the aid of a mortgage.

Do you agree?

(Paragraphs 8.11, 8.12)

11.38 Do you agree with our provisional recommendation that these proposed powers should—

(1) apply to trusts whether they were created before or after any legislation was brought into force unless a contrary intention was expressed in the instrument creating the trust; and

[1] Such trustees already have the powers proposed or something similar.

(2) be in addition to any more limited powers to purchase land that have either been—

(a) conferred by the instrument creating the trust; or

(b) previously granted by the court or the Charity Commissioners?

(Paragraph 8.13)

POWER TO INSURE

11.39 Do you agree that, for the purpose of exercising their functions as trustees, all trustees should have the same power to insure the trust property as they would if they were the absolute owners of it? If you disagree, do you consider that the power should be more limited or that the trustees' obligations should be more fully spelt out, and if so, in what respects?

(Paragraph 9.18)

11.40 We recommend that trustees should be under a duty to insure trust property—

(1) in circumstances when;

(2) against such risks as; and

(3) for such amount as;

a reasonable prudent person would have insured the property. Do you agree?

(Paragraph 9.21)

11.41 Do you agree with our provisional recommendation that—

(1) both the statutory power and the statutory duty to insure which we propose should apply where property is held either—

(a) on a bare trust for a beneficiary absolutely; or

(b) for beneficiaries who are of full age and capacity and, taken together, are absolutely entitled to the trust property; but

(2) in those circumstances, if the beneficiaries all agree, they should be able to direct the trustees not to insure the property?

(Paragraph 9.23)

11.42 Do you agree with our provisional recommendation that where trust property has been vested by trustees in nominees, the trustees should have power to direct the nominees that they shall not insure the property?

(Paragraph 9.25)

11.43 Do you agree with our provisional recommendation that trustees should have a discretion to apportion the payment of premiums between income and capital as they think fit?

(Paragraph 9.26)

11.44 Do you agree that, subject to any expression of contrary intention in the instrument creating the trust—

(1) the powers and duties which we propose in relation to insurance should apply to all trusts, whenever created, in addition to any powers conferred by the trust instrument; and

(2) the duty to insure which we propose in paragraph 11.40 above should also apply where trustees insure the trust property under an express power in the trust instrument?

If you do not agree, what limitations would you place upon the applicability of the proposed powers and duties?

(Paragraph 9.29)

PROFESSIONAL CHARGING CLAUSES

11.45 Do you agree with our provisional recommendation that there should be an implied statutory charging clause and that it should apply—

(1) in relation to all trusts (other than pension trusts and charitable trusts) and to the unadministered estates of all deceased persons except—

(a) where there is a direction to the contrary in the will or trust instrument (but not merely some limitation on remuneration); or

(b) where some other benefit or remuneration is provided in the will or trust instrument;

(2) whether the trust arose or the deceased person died before or after any legislation was brought into force; and

(3) notwithstanding, but subject to, any previous order by a court which has authorised the trustees or personal representatives to be remunerated for any work?

11.46 If you agree that there should be such a charging clause, do you agree with our provisional recommendation that—

(1) the charging clause should permit any trustee or personal representative who is also engaged in a profession or business to charge and be paid out of the trust property for any business or act done, advice given, or time expended in connection with the trust;

(2) the power to charge in (1) should apply whether or not the matter was one

which a trustee not being a professional could have undertaken; and

(3) those charges should be reasonable and should not exceed the amount which the trustee would charge for such work in the ordinary course of his or her business or profession?

If you do not agree with the terms which we propose, in what respects do you consider that they should be modified?

(Paragraphs 10.26, 10.27)

11.47 Do you consider whether, in relation to—

(1) pension trusts; and

(2) charitable trusts;

the statutory charging clause that we have proposed—

(a) should apply;

(b) should be wholly inapplicable; or

(c) should not apply automatically, but the trustees should have power to authorise one (or more) of their number to charge for his or her services in accordance with the clause?

(Paragraph 10.28)

11.48 Do you agree with our provisional recommendation that—

(1) a charging clause should no longer be regarded as a conditional gift or legacy but as remuneration;

(2) any sum due under such a clause should be an expense of administering the trust or estate;

(3) this proposal should only apply to trusts created or to the estates of persons dying after any legislation which implemented these recommendations was brought into force?

(Paragraph 10.30)

11.49 We provisionally recommend that—

(1) a professional charging clause should be taken to permit a trustee to charge for work and services properly rendered for the trust, whether or not that work or those services could have been provided by a lay trustee, unless the trust instrument provides to the contrary; and

(2) this provision should apply to all professional charging clauses in wills and trusts, whenever made.

Do you agree?

(Paragraph 10.32)

APPENDIX A
EXTRACTS FROM THE PRINCIPAL STATUTES AND OTHER MATERIALS REFERRED TO IN THE PAPER

Relevant extracts from the following provisions:

Public Trustee Act 1906, section 4
Trustee Act 1925, sections 7, 19, 21, 23, 25, and 30
Charities Act 1993, section 26
Charity Commissioners' Model Order under section 26 of the Charities Act 1993 (reproduced by kind permission of the Charity Commissioners)
Pensions Act 1995, sections 34, 35 and 36

Public Trustee Act 1906

Custodian trustee

4. (1) Subject to rules under this Act the public trustee may, if he consents to act as such, and whether or not the number of trustees has been reduced below the original number, be appointed to be custodian trustee of any trust—

(a) by order of the court made on the application of any person on whose application the court may order the appointment of a new trustee; or

(b) by the testator, settlor, or other creator of any trust; or

(c) by the person having the power to appoint new trustees.

(2) Where the public trustee is appointed to be custodian trustee of any trust—

(a) The trust property shall be transferred to the custodian trustee as if he were sole trustee, and for that purpose vesting orders may, where necessary, be made under the Trustee Act [1925]:

(b) The management of trust property and the exercise of any power or discretion exercisable by the trustees under the trust shall remain vested in the trustees other than the custodian trustee (which trustees are hereinafter referred to as the managing trustees):

(c) As between the custodian trustee and the managing trustees, and subject and without prejudice to the rights of any other persons, the custodian trustee shall have the custody of all securities and documents of title relating to the trust property, but the managing trustee shall have free access thereto and be entitled to take copies thereof or extracts therefrom:

(d) The custodian trustee shall concur in and perform all acts necessary to enable the managing trustees to exercise their powers of management or any other power or discretion vested in them (including the power to pay money or securities into court), unless the matter in which he is requested to concur is a breach of trust, or involves a personal liability upon him in respect of calls or otherwise, but, unless he so concurs, the custodian trustee shall not be liable for any act or default on the part of the managing trustees or any of them:

(e) All sums payable to or out of the income or capital of the trust property shall be paid to the custodian trustee: Provided that the custodian trustee may

allow the dividends and other income derived from the trust property to be paid to the managing trustees or to such person as they direct, or into such bank to the credit of such person as they may direct, and in such case shall be exonerated from seeing to the application thereof and shall not be answerable for any loss or misapplication thereof:

(f) The power of appointing new trustees, when exercisable by the trustees, shall be exercisable by the managing trustees alone, but the custodian trustee shall have the same power of applying to the court for the appointment of a new trustee as any other trustee:

(g) In determining the number of trustees for the purposes of the Trustee Act [1925], the custodian trustee shall not be reckoned as a trustee:

(h) The custodian trustee, if he acts in good faith, shall not be liable for accepting as correct and acting upon the faith of any written statement by the managing trustees as to any birth, death, marriage, or other matter of pedigree or relationship, or other matter of fact, upon which the title to the trust property or any part thereof may depend, nor for acting upon any legal advice obtained by the managing trustees independently of the custodian trustee:

(i) The court may, on the application of either the custodian trustee, or any of the managing trustees, or of any beneficiary, and on proof to their satisfaction that it is the general wish of the beneficiaries, or that on other grounds it is expedient, to terminate the custodian trusteeship, make an order for that purpose, and the court may thereupon make such vesting orders and give such directions as under the circumstances may seem to the court to be necessary or expedient.

(3) The provisions of this section shall apply in like manner as to the public trustee to any banking or insurance company or other body corporate entitled by rules made under this Act to act as custodian trustee, with power for such company or body corporate to charge and retain or pay out of the trust property fees not exceeding the fees chargeable by the public trustee as custodian trustee.

Trustee Act 1925

Investment in bearer securities

7. (1) A trustee may, unless expressly prohibited by the instrument creating the trust, retain or invest in securities payable to bearer which, if not so payable, would have been authorised investments:

Provided that securities to bearer retained or taken as an investment by a trustee (not being a trust corporation) shall, until sold, be deposited by him for safe custody and collection of income with a banker or banking company.

A direction that investments shall be retained or made in the name of a trustee shall not, for the purposes of this subsection, be deemed to be such an express prohibition as aforesaid.

(2) A trustee shall not be responsible for any loss incurred by reason of such deposit, and any sum payable in respect of such deposit and collection shall be paid out of the income of the trust property.

Power to insure [as amended by the Trusts of Land and Appointment of Trustees Act 1996]

19. (1) A trustee may insure any personal property against loss or damage to any amount, including the amount of any insurance already on foot, not exceeding three fourth parts of the full value of the property, and pay the premiums for such insurance out of the income thereof or out of any income of any other property subject to the same trusts without obtaining the consent of any person who may be entitled wholly or partly to such income.

(2) This section does not apply to any personal property which a trustee is bound forthwith to convey absolutely to any beneficiary upon being requested to do so.

Deposit of documents for safe custody

21. Trustees may deposit any documents held by them relating to the trust, or to the trust property, with any banker or banking company or any other company whose business includes the undertaking of the safe custody of documents, and any sum payable in respect of such deposit shall be paid out of the income of the trust property.

Power to employ agents

23. (1) Trustees or personal representatives may, instead of acting personally, employ and pay an agent, whether a solicitor, banker, stockbroker, or other person, to transact any business or do any act required to be transacted or done in the execution of the trust, or the administration of the testator's or intestate's estate, including the receipt and payment of money, and shall be entitled to be allowed and paid all charges and expenses so incurred, and shall not be responsible for the default of any such agent if employed in good faith.

(2) Trustees or personal representatives may appoint any person to act as their agent or attorney for the purpose of selling, converting, collecting, getting in, and executing and perfecting insurances of, or managing or cultivating, or otherwise administering any property, real or personal, moveable or immoveable, subject to the trust or forming part of the testator's or intestate's estate, in any place outside the United Kingdom or executing or exercising any discretion or trust or power vested in them in relation to any such property, with such ancillary powers, and with and subject to such provisions and restrictions as they may think fit, including a power to appoint substitutes, and shall not, by reason only of their having made such appointment, be responsible for any loss arising thereby.

(3) Without prejudice to such general power of appointing agents as aforesaid—

(a) A trustee may appoint a solicitor to be his agent to receive and give a discharge for any money or valuable consideration or property receivable by the trustee under the trust, by permitting the solicitor to have the custody of, and to produce, a deed having in the body thereof or endorsed thereon a receipt for such money or valuable consideration or property, the deed being executed, or the endorsed receipt being signed, by the person entitled to give a receipt for that consideration;

(b) A trustee shall not be chargeable with breach of trust by reason only of his having made or concurred in making any such appointment; and the production of any such deed by the solicitor shall have the same statutory validity and effect as if the person appointing the solicitor had not been a trustee;

(c) A trustee may appoint a banker or solicitor to be his agent to receive and give a discharge for any money payable to the trustee under or by virtue of a policy of insurance, by permitting the banker or solicitor to have the custody of and to produce the policy of insurance with a receipt signed by the trustee, and a trustee shall not be chargeable with a breach of trust by reason only of his having made or concurred in making any such appointment;

Provided that nothing in this subsection shall exempt a trustee from any liability which he would have incurred if this Act and any enactment replaced by this Act had not been passed, in case he permits any such money, valuable consideration, or property to remain in the hands or under the control of the banker or solicitor for a period longer than is reasonably necessary to enable the banker or solicitor, as the case may be, to pay or transfer the same to the trustee.

This subsection applies whether the money or valuable consideration or property was or is received before or after the commencement of this Act.

Power to delegate trusts during absence abroad [as amended by the Powers of Attorney Act 1971]

25. (1) Notwithstanding any rule of law or equity to the contrary, a trustee may, by power of attorney, delegate for a period not exceeding twelve months the execution or exercise of all or any of the trusts, powers and discretions vested in him as trustee either alone or jointly with any other person or persons.

(2) The persons who may be donees of a power of attorney under this section include a trust corporation but not (unless a trust corporation) the only other co-trustee of the donor of the power.

(3) An instrument creating a power of attorney under this section shall be attested by at least one witness.

(4) Before or within seven days after giving a power of attorney under this section the donor shall give written notice thereof (specifying the date on which the power comes into operation and its duration, the donee of the power, the reason why the power is given and, where some only are delegated, the trusts, powers and discretions delegated) to—

(a) each person (other than himself), if any, who under any instrument creating the trust has power (whether alone or jointly) to appoint a new trustee; and

(b) each of the other trustees, if any;

but failure to comply with this subsection shall not, in favour of a person dealing with the donee of the power, invalidate any act done or instrument executed by the donee.

(5) The donor of a power of attorney given under this section shall be liable for the acts or defaults of the donee in the same manner as if they were the acts or defaults of the donor.

(6) For the purpose of executing or exercising the trusts or powers delegated to him, the donee may exercise any of the powers conferred on the donor as trustee by statute or by the instrument creating the trust, including power, for the purpose of the transfer of any inscribed stock, himself to delegate to an attorney power to transfer but not including the power of delegation conferred by this section.

(7) The fact that it appears from any power of attorney given under this section, or from any evidence required for the purposes of any such power of attorney or otherwise, that in dealing with any stock the donee of the power is acting in the execution of a trust shall not be deemed for any purpose to affect any person in whose books the stock is inscribed or registered with any notice of the trust.

(8) This section applies to a personal representative, tenant for life and statutory owner as it applies to a trustee except that subsection (4) shall apply as if it required the notice there mentioned to be given—

(a) in the case of a personal representative, to each of the other personal representatives, if any, except any executor who has renounced probate;

(b) in the case of a tenant for life, to the trustees of the settlement and to each person, if any, who together with the person giving the notice constitutes the tenant for life;

(c) in the case of a statutory owner, to each of the persons, if any, who together with the person giving the notice constitute the statutory owner and, in the case of a statutory owner by virtue of section 23(1)(a) of the Settled Land Act 1925, to the trustees of the settlement.

Implied indemnity of trustees

30. (1) A trustee shall be chargeable only for money and securities actually received by him notwithstanding his signing any receipt for the sake of conformity, and shall be answerable and accountable only for his own acts, receipts, neglects, or defaults, and not for those of any other trustee, nor for any banker, broker, or other person with whom any trust money or securities may be deposited, nor for the insufficiency or deficiency of any securities, nor for any other loss, unless the same happens through his own wilful default.

(2) A trustee may reimburse himself or pay or discharge out of the trust premises all expenses incurred in or about the execution of the trusts or powers.

Charities Act 1993, section 26

Power to authorise dealings with charity property etc

26. (1) Subject to the provisions of this section, where it appears to the Commissioners that any action proposed or contemplated in the administration of a charity is expedient in the interests of the charity, they may by order sanction that action, whether or not it would otherwise be within the powers exercisable by the charity trustees in the administration of the charity; and anything done under the authority of such an order shall be deemed to be properly done in the exercise of those powers.

(2) An order under this section may be made so as to authorise a particular transaction, compromise or the like, or a particular application of property, or so as to give a more general authority, and (without prejudice to the generality of subsection (1) above) may authorise a charity to use common premises, or employ a common staff, or otherwise combine for any purpose of administration, with any other charity.

(3) An order under this section may give directions as to the manner in which any expenditure is to be borne and as to other matters connected with or arising out of the action thereby authorised; and where anything is done in pursuance of an authority given by any such order, any directions given in connection therewith shall be binding on the charity trustees for the time being as if contained in the trusts of the charity; but any such directions may on the application of the charity be modified or superseded by a further order.

(4) Without prejudice to the generality of subsection (3) above, the directions which may be given by an order under this section shall in particular include directions for meeting any expenditure out of a specified fund, for charging any expenditure to capital or to income, for requiring expenditure charged to capital to be recouped out of income within a specified period, for restricting the costs to be incurred at the expense of the charity, or for the investment of moneys arising from any transaction.

(5) An order under this section may authorise any act notwithstanding that it is prohibited by any of the disabling Acts mentioned in subsection (6) below or that the trusts of the charity provide for the act to be done by or under the authority of the court; but no such order shall authorise the doing of any act expressly prohibited by Act of Parliament

other than the disabling Acts or by the trusts of the charity or shall extend or alter the purposes of the charity.

(6) The Acts referred to in subsection (5) above as the disabling Acts are the Ecclesiastical Leases Act 1571, the Ecclesiastical Leases Act 1572, the Ecclesiastical Leases Act 1575 and the Ecclesiastical Leases Act 1836.

(7) An order under this section shall not confer any authority in relation to a building which has been consecrated and of which the use or disposal is regulated, and can be further regulated, by a scheme having effect under the Union of Benefices Measures 1923 to 1952, the Reorganisation Areas Measures 1944 and 1954, the Pastoral Measure 1968 or the Pastoral Measure 1983, the reference to a building being taken to include part of a building and any land which under such a scheme is to be used or disposed of with a building to which the scheme applies.

Charity Commissioners' Model Order under section 26 of the Charities Act 1993

Delegation to an investment manager (clauses 1 to 4) and appointment of a nominee (clause 5).

1. The Trustees may appoint as the investment manager for the Charity a person who they are satisfied after inquiry is a proper and competent person to act in that capacity and who is either:

(i) an individual of repute with at least fifteen years' experience of investment management who is an authorised person within the meaning of the Financial Services Act 1986 or

(ii) a company or firm of repute which is an authorised or exempted person within the meaning of that Act otherwise than by virtue of s 45(1)(j) of that Act;

2. The Trustees may delegate to an investment manager so appointed power at his discretion to buy and sell investments for the Charity on behalf of the Trustees in accordance with the investment policy laid down by the Trustees. The Trustees may do so only on terms consistent with this Order.

3. Where the Trustees make any delegation under this Order they shall:

(a) inform the investment manager in writing of the extent of the Charity's investment powers;

(b) lay down a detailed investment policy for the Charity and immediately inform the investment manager in writing of it and of any changes to it;

(c) ensure that the terms of the delegated authority are clearly set out in writing and notified to the investment manager;

(d) ensure that they are kept informed and review on a regular basis the performance of their investment portfolio managed by the investment manager and on the exercise by him of his delegated authority;

(e) take all reasonable care to ensure that the investment manger complies with the terms of the delegated authority; and

(f) review the appointment at such intervals not exceeding 24 months as they

think fit.

4. Where the Trustees make any delegation under this Order they shall do so on the terms that:

(a) the investment manager shall comply with the terms of his delegated authority;

(b) the investment manager shall not do anything which the Trustees do not have the power to do;

(c) the Trustees may with reasonable notice revoke the delegation or vary any of its terms in a way which is consistent with the terms of this Order; and

(d) the Trustees shall give directions to the investment manager as to the manner in which he is to report to them all sales and purchases of investments made on their behalf.

5. The Trustees may:

(a) make such arrangements as they think fit for any investments of the Charity or income from those investments to be held by a corporate body as the Trustees' nominee; and

(b) pay reasonable and proper remuneration to any corporate body acting as the Trustees' nominee in pursuance of this clause.

Pensions Act 1995, sections 34 - 36

Power of investment and delegation

34. (1) The trustees of a trust scheme have, subject to any restriction imposed by the scheme, the same power to make an investment of any kind as if they were absolutely entitled to the assets of the scheme.

(2) Any discretion of the trustees of a trust scheme to make any decision about investments—

(a) may be delegated by or on behalf of the trustees to a fund manager to whom subsection (3) applies to be exercised in accordance with section 36, but

(b) may not otherwise be delegated except under section 25 of the Trustee Act 1925 (delegation of trusts during absence abroad) or subsection (5) below.

(3) This subsection applies to a fund manager who, in relation to the decisions in question, falls, or is treated as falling, within any of paragraphs (a) to (c) of section 191(2) of the Financial Services Act 1986 (occupational pension schemes: exemptions where decisions taken by authorised and other persons).

(4) The trustees are not responsible for the act or default of any fund manager in the exercise of any discretion delegated to him under subsection (2)(a) if they have taken all such steps as are reasonable to satisfy themselves or the person who made the delegation on their behalf has taken all such steps as are reasonable to satisfy himself—

(a) that the fund manager has the appropriate knowledge and experience for managing the investments of the scheme, and

(b) that he is carrying out his work competently and complying with section 36.

(5) Subject to any restriction imposed by a trust scheme—

(a) the trustees may authorise two or more of their number to exercise on their behalf any discretion to make any decision about investments, and

(b) any such discretion may, where giving effect to the decision would not constitute carrying on investment business in the United Kingdom (within the meaning of the Financial Services Act 1986), be delegated by or on behalf of the trustees to a fund manager to whom subsection (3) does not apply to be exercised in accordance with section 36;

but in either case the trustees are liable for any acts or defaults in the exercise of the discretion if they would be so liable if they were the acts or defaults of the trustees as a whole.

(6) Section 33 does not prevent the exclusion or restriction of any liability of the trustees of a trust scheme for the acts or defaults of a fund manager in the exercise of a discretion delegated to him under subsection (5)(b) where the trustees have taken all such steps as are reasonable to satisfy themselves, or the person who made the delegation on their behalf has taken all such steps as are reasonable to satisfy himself—

(a) that the fund manager has the appropriate knowledge and experience for managing the investments of the scheme, and

(b) that he is carrying out his work competently and complying with section 36;

and subsection (2) of section 33 applies for the purposes of this subsection as it applies for the purposes of that section.

(7) The provisions of this section override any restriction inconsistent with the provisions imposed by any rule of law or by or under any enactment, other than an enactment contained in, or made under, this Part or the Pension Schemes Act 1993.

Investment principles

35. (1) The trustees of a trust scheme must secure that there is prepared, maintained and from time to time revised a written statement of the principles governing decisions about investments for the purposes of the scheme.

(2) The statement must cover, among other things—

(a) the trustees' policy for securing compliance with sections 36 and 56, and

(b) their policy about the following matters.

(3) Those matters are—

(a) the kinds of investments to be held,

(b) the balance between different kinds of investments,

(c) risk,

(d) the expected return on investments,

(e) the realisation of investments, and

(f) such other matters as may be prescribed.

(4) Neither the trust scheme nor the statement may impose restrictions (however expressed) on any power to make investments by reference to the consent of the employer.

(5) The trustees of a trust scheme must, before a statement under this section is prepared or revised—

(a) obtain and consider the written advice of a person who is reasonably believed by the trustees to be qualified by his ability in and practical experience of financial matters and to have the appropriate knowledge and experience of the management of the investments of such schemes, and

(b) consult the employer.

(6) If in the case of any trust scheme—

(a) a statement under this section has not been prepared or is not being maintained, or

(b) the trustees have not obtained and considered advice in accordance with subsection (5),

sections 3 and 10 apply to any trustee who has failed to take all such steps as are reasonable to secure compliance.

(7) This section does not apply to any scheme which falls within a prescribed class or description.

Choosing investments

36. (1) The trustees of a trust scheme must exercise their powers of investment in accordance with subsections (2) to (4) and any fund manager to whom any discretion has been delegated under section 34 must exercise the discretion in accordance with subsection (2).

(2) The trustees or fund manager must have regard—

(a) to the need for diversification of investments, in so far as appropriate to the circumstances of the scheme, and

(b) to the suitability to the scheme of investments of the description of investment proposed and of the investment proposed as an investment of that description.

(3) Before investing in any manner (other than in a manner mentioned in Part I of Schedule 1 to the Trustee Investments Act 1961) the trustees must obtain and consider proper advice on the question whether the investment is satisfactory having regard to the matters mentioned in subsection (2) and the principles contained in the statement under section 35.

(4) Trustees retaining any investment must—

(a) determine at what intervals the circumstances, and in particular the nature of the investment, make it desirable to obtain such advice as is mentioned in subsection (3), and

(b) obtain and consider such advice accordingly.

(5) The trustees, or the fund manager to whom any discretion has been delegated

under section 34, must exercise their powers of investment with a view to giving effect to the principles contained in the statement under section 35, so far as reasonably practicable.

(6) For the purposes of this section "proper advice" means—

(a) where giving the advice constitutes carrying on investment business in the United Kingdom (within the meaning of the Financial Services Act 1986), advice—

(i) given by a person authorised under Chapter III of Part I of that Act,

(ii) given by a person exempted under Chapter IV of that Part who, in giving the advice, is acting in the course of the business in respect of which he is exempt,

(iii) given by a person where, by virtue of paragraph 27 of Schedule 1 to that Act, paragraph 15 of that Schedule does not apply to giving the advice, or

(iv) given by a person who, by virtue of regulation 5 of the Banking Coordination (Second Council Directive) Regulations 1992, may give the advice though not authorised as mentioned in sub-paragraph (i) above.

(b) in any other case, the advice of a person who is reasonably believed by the trustees to be qualified by his ability in and practical experience of financial matters and to have the appropriate knowledge and experience of the management of the investments of trust schemes.

(7) Trustees shall not be treated as having complied with subsection (3) or (4) unless the advice was given or has subsequently been confirmed in writing.

(8) If the trustees of a trust scheme do not obtain and consider advice in accordance with this section, sections 3 and 10 apply to any trustee who has failed to take all such steps as are reasonable to secure compliance.

APPENDIX B
MEMBERS OF THE TRUST LAW COMMITTEE

Chairman
Sir John Vinelott

Deputy Chairman
Professor David Hayton

Secretary
John Dilger

Committee
Judge Paul Baker QC
Millie Brenninkmeyer
The Hon Mark Bridges
Professor Edward Burn
Martin Day
Robin Ellison
Martyn Frost
Sir William Goodhart QC
Judith Ingham
Michael Jacobs
Simon Jennings
David Long
Victoria Love
Christopher McCall QC
Professor Jill Martin
John Mowbray QC
Richard Nolan
Edward Nugee QC
Hubert Picarda QC
David Pollard
John Quarrell
Geoffrey Shindler
Professor Adrian Shipwright
William Swadling
Mr Justice Walker
Nicholas Warren QC
Philip R Wood

Observers
Charles Harpum
Robert Venables